Supreme Court, U.S.
FILED
JUL 15 2002
OFFICE OF THE CLERK

No. 02-73

In the Supreme Court of the United States

STUDENT LOAN FUND OF IDAHO, INC.
Petitioner,

v.

UNITED STATES DEPARTMENT OF EDUCATION,
AND
RODERICK R. PAIGE, IN HIS OFFICIAL CAPACITY AS
SECRETARY OF THE UNITED STATES
DEPARTMENT OF EDUCATION,
Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

In 1976, responding to the failing Federally Insured Student Loan Program ("FISLP"), the U.S. Congress amended the Higher Education Act of 1965 to encourage greater participation by private and State entities in providing financial aid to college students. The U.S. Secretary of Education, as authorized by Congress, offered several financial incentives to private non-profit corporations and State agencies to entice their participation as guaranty agencies in the Guaranteed Student Loan Programs. To the extent these private and State organizations could adequately cover student loan needs in their respective states, the FISLP was placed on standby. In 1978, the Student Loan Fund of Idaho, Inc. ("SLFI") was designated by Idaho's Governor to be the guaranty agency for the State of Idaho. Shortly thereafter SLFI entered into contracts with the Secretary of Education (then Commissioner of Education) to obtain the benefits of the Guaranteed Student Loan Programs for the State of Idaho, Idaho's students and itself. SLFI then executed contracts (to which the Secretary was not a party) with numerous lenders in the State of Idaho promising to guarantee such lenders against student defaults.

In this context, the questions presented are:

1. Whether common-law rules of contract construction, including the longstanding rule of *contra proferentem*, apply to government-drawn contracts, and, if so, to what effect.

2. Whether a government agency's informal and inconsistent interpretation of its own regulations is entitled to *Chevron* deference.

3. Whether basic contract and property rights are lost when a private non-profit entity enters into contracts with the Federal government.

PARTIES TO THE PROCEEDING AND CORPORATE STATEMENT

Petitioner

Petitioner is the Student Loan Fund of Idaho, Inc., a private non-profit corporation charged to promote educational opportunities for Idaho students. SLFI was the Plaintiff in the District Court, and the Appellee/Cross Appellant in the Ninth Circuit Court of Appeals. SLFI is not a publicly traded company. There is no parent or publicly held company owning 10% or more of the corporation's stock. SLFI has no affiliates or subsidiaries.

Respondents

Respondents are Roderick M. Paige,[1] United States Secretary of Education, and the United States Department of Education. Respondents were the Defendants in the District Court, and the Appellant/Cross Appellee before the Ninth Circuit Court of Appeals.

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[1] Roderick R. Paige was substituted for his predecessor, Richard W. Riley, as Secretary of the United States Department of Education.

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PETITION FOR WRIT OF CERTIORARI

Petitioner respectfully petitions for a Writ of Certiorari to review the opinion of the Ninth Circuit Court of Appeals in this case.

OPINIONS BELOW

The Ninth Circuit Court of Appeals opinion, (Appendix ("App.") B at 3a), is reported at 272 F.3d 1155 (9th Cir. 2001). The amended opinion is reported at 289 F.3d 599 (9th Cir. 2002). The opinions and final judgment of the United States District Court for the District of Idaho, App. D & E, at 34a - 91a, are unreported. The 1996 Memorandum Decision of the Ninth Circuit Court of Appeals, App. G at 94a, is unreported.

JURISDICTION

The District Court's jurisdiction was invoked pursuant to 28 U.S.C. §1331. The opinion of the Ninth Circuit Court of Appeals was entered on December 4, 2001. The Court of Appeals entered an amended opinion and order denying a timely petition for rehearing and rehearing en banc on April 15, 2002. The jurisdiction of this court is invoked pursuant to 28 U.S.C. §1254(1).

STATUTORY AND REGULATORY PROVISIONS INVOLVED

The Higher Education Act of 1965, as amended (the "HEA"), 20 U.S.C. §§ 1001 et seq. and corresponding Federal Regulations, 34 C.F.R. 682.100 et seq. Selected provisions (as they existed on June 30, 1994, with the exception of 20 U.S.C. §1072(e) which was repealed prior

thereto) are reprinted in the Appendix. App. H at 99a-110a.

INTRODUCTION AND STATEMENT

This case presents the issue of how government-drawn contracts between a private party and the Federal government are to be interpreted. This issue arises in the context of contracts between a private non-profit entity and the U.S. Secretary of Education (the "Secretary") for making guaranteed student loans available to college students.

Guaranty agencies extend their own loan guarantees to lenders whereby the guaranty agencies become primarily (and until enactment of 20 U.S.C. §1082(o) in 1992, solely) liable to insure lenders against losses due to borrower defaults. These guarantees are made in reliance on the government's promise to pay reinsurance. Although one can imagine cases in which the potential gain might induce a party to assume a substantial risk or liability, "It would, indeed, have been madness for [guaranty agencies] to have engaged in these transactions with no more protection than the Government's reading would have given them, for the very existence of their institutions would then have been in jeopardy from the moment their agreements were signed." *United States v. Winstar Corporation et al.*, 518 U.S. 839, 116 S.Ct. 2432, 135 L.Ed.2d 964, 1013 (1996).

The reinsurance contracts (drafted by the Department of Education, "Department") provide that SLFI could terminate the contracts upon notice but limited termination by the Secretary to "for cause." App. J at 125a; K at 133a-34a. The HEA grants the guaranty agency a contractual right to reimbursement during the life of the loan. Consistent therewith, the contracts expressly provide that the Secretary's obligation to pay reinsurance on loans insured by SLFI prior to termination shall not be effected by termination. In the

instant case, there have been no statutory or regulatory enactments which have changed the terms of the contracts between SLFI and the Secretary in any matter material to termination or reinsurance.

Despite the terms of the contracts with respect to termination and rights of the parties, the Ninth Circuit and the Secretary posit that if a fully performing private entity elects to terminate its contracts in accordance with their terms, the Secretary may take action against such entity under statutory remedial provisions for wrong-doing or non-performance without regard to whether such wrong-doing or nonperformance actually exists. As construed by the Ninth Circuit and the Secretary, such entities are merely "servants of the Federal government" who must "bow to the Secretary's directives."

Interpreting the contract provisions with respect to the Secretary's reinsurance obligation and termination, which it held to be ambiguous, the Ninth Circuit created its own rule to resolve ambiguities. In doing so, the Ninth Circuit gave deference to an interpretation of the Secretary first announced in the context of this litigation and unheard of in the statutes, regulations or other pronouncements. The contract ambiguity rule the Ninth Circuit should have applied is that enunciated by the Supreme Court and the Federal Circuit to the effect that latent ambiguities in government contracts are to be constructed against the government as drafter.

There is no logical way to reconcile the conflict between the Ninth Circuit opinion and the prior opinions of this Court and the Court of Appeals for the Federal Circuit. If the Ninth Circuit and the Secretary are correct in these assertions and if such positions become commonly known the days of mutual cooperative agreements between the federal government and private entities are over (as well they should

be). For these reasons, review by this Court is not only warranted but necessary.

I. THE STATUTORY/REGULATORY FRAMEWORK

In 1965, the Congress enacted the HEA providing for a Federal loan insurance program ("FISLP"), "on a standby basis," operational only in the event that the demand for guaranteed student loans at any institution of higher education was not met by a State and/or private nonprofit loan insurance program. App. H at 99a. By late 1968, the FISLP was operating in about one-half of the states. To encourage participation of private and state guaranty agencies, Congress amended the HEA to provide guaranty agencies reinsurance of a portion of the principal amount of losses due to borrower defaults.

The Education Amendments of 1976, amended the HEA partially in response to criticism of the Federal administration of the student loan program and to encourage greater participation from State and private nonprofit guarantors. S.Rep. No. 94-882, 94th Cong. 2nd Sess. vol. 4, 20-25 (1976), *reprinted in* 1976 U.S.C.C.A.N. 4732-4737(*see* particularly the letter therein of Senators Nunn and Percy on behalf of the Government Operations Committee, pp. 4733-4735). App. I at 111a-117a. These amendments directed the Commissioner (now Secretary) of Education to offer several financial incentives to State and private nonprofit guarantors to induce their participation in the guaranteed student loan programs. 20 U.S.C. §1078(c)(1)(A) authorizes the Secretary to enter into reinsurance contracts with State and private nonprofit guaranty agencies and provides, in part, that:

> "The Secretary may enter into a guaranty agreement with any guaranty agency, whereby the Secretary shall undertake to reimburse it, under such terms and conditions as the Secretary may establish, with respect to losses (resulting from the default of the student borrower) on the unpaid balance of the principal and accrued interest of any insured loan. **The guaranty agency shall, be deemed to have a contractual right against the United States, during the life of such loan, to receive reimbursement according to the provisions of this subsection**. Upon receipt of an accurate and complete request by a guaranty agency for reimbursement with respect to such losses, the Secretary shall pay promptly and without administrative delay." (Emphasis added). *Id.* App. H at 104a.

Fourteen years after SLFI's guarantee activities commenced and in response to the financial collapse of one of the nation's largest private nonprofit guarantors in 1991, Congress amended the HEA authorizing the Secretary to pay lender default claims *if the guarantor is unable to pay* (*See* 20 U.S.C. §1082(o), App. H at 108a) and to take other actions with respect to an insolvent guarantor for minimizing government losses. *See* 20 U.S.C. §§ 1078(c)(9)(E) & (F), App. H at 105a-107a; H.Rep. No. 102-447, 102nd Cong., 2nd Sess. vol. 4, 42-43 (1992) *reprinted in* 1992 U.S.C.C.A.N. 375-76, App. I at 118a-119a; H.Conf.Rep. No. 102-630, 102nd Cong., 2nd Sess. vol. 4, 463 (1992) *reprinted in* 1992 U.S.C.C.A.N. 578.

About the same time, Congress amended the HEA in 1992, responding to the so-called "spend down" litigation (discussed below), to provide that the unencumbered non-

Federal portion of guarantor reserve funds and assets are not subject to "recall, repayment, or recovery by the Secretary" except in cases of guarantor insolvency. 20 U.S.C. §1072(a)(2).[2] App. H at 100a-101a. In the following year, Congress added §1072(g) to the HEA allowing that under certain specified circumstances the Secretary may direct the transfer of a guarantor's "Federal portion" of reserve funds. *See* 20 U.S.C. §1072(g)(1), App. H at 103a; H.Conf.Rep. No. 103-213, 103rd Cong., 1st Sess. vol. 3, 455-456 (1993) *reprinted in* 1993 U.S.C.C.A.N. 1144-45, App. I at 119a-120a.

II. THE LITIGATION

A. The U.S. District Court Pre-Trial Litigation

The contracts entered into in 1978 between SLFI and the Secretary provide for the payment of reinsurance to SLFI on all loans insured by SLFI. App. J at 125a; K at 133a-134a. The authorizing statute provides that "The guaranty agency shall be deemed to have a contractual right against the United States, for the life of such loan to receive reimbursement . . ." 20 U.S.C. §1078(c)(1)(A), App. H at 104a. Relying on this promise by Congress and the Secretary, SLFI entered into contracts (to which the

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[2] The spend down cases arose out of a self-repealing provision of the HEA, former 20 U.S.C. §1072(e), which contained a series of definitions to determine the existence of "excess cash reserves." Rather than defer to the regulations of the Department, Congress directed that implementation be based upon guidelines of the General Accounting Office referenced herein at page 19. *See Education Assistance Corp. v. Cavazos*, *infra*, at footnote 9. At trial, SLFI demonstrated the inapplicability of the spend down rationale. App. E at 74a.

Department was not a party) with Idaho lenders to insure them against default by the student loan borrowers. From 1978 to June 30, 1994, SLFI guaranteed over $400 million in student loans. SLFI remains contractually obligated to these lenders to insure all guaranteed loans still outstanding and SLFI continues to fulfill these obligations.

In 1993, financial incentives provided by the government to guaranty agencies were cut and reinsurance rates were reduced. In this context, SLFI opted to discontinue guaranteeing new student loans but continue fulfilling all guaranty agency functions as to loans previously insured. App. M at 142a. This ability to terminate the contracts without effecting obligations already in place is expressly authorized by the Department-drafted contracts.

In response to SLFI's prospective termination of the contracts, the Department ordered SLFI to cease all operations and transfer all of its funds and assets to another guaranty agency. App. N at 143a-146a. SLFI brought suit to enforce its rights under the contracts and to enjoin the Department from enforcing what SLFI perceives as unauthorized demands of the Department. Summary Judgment was initially granted to the Secretary and SLFI was ordered to transfer its "reserve funds" as directed by the Department pursuant to 20 U.S.C. §1072(g).

B. On Appeal from Summary Judgment

On appeal from Summary Judgment in 1996, the Court of Appeals held that the Department's directives purportedly authorized under 20 U.S.C. §1072(g)(1) did not satisfy the prerequisite requirements of the statute. Accordingly, the Court reversed and remanded the case to the District Court. App. G at 94a-98a.

C. Trial and Opinion of the U.S. District Court

In October 1998, a nine day trial was held on SLFI's contract claims and the Department's counterclaims for enforcement of its directives ordering SLFI to transfer all of its funds and assets to the Department or its designee. In an opinion issued in August 1999, the District Court held that the agreements between the parties were enforceable contracts, that any Federal funds held by SLFI had been properly expended on guaranty agency purposes and that obligations (of each party) in place at the time of termination survived voluntary termination. App. E at 56a-91a. Accordingly, the District Court awarded SLFI approximately $16.5 million in contract damages based upon the Secretary's failure to pay reinsurance. App. F at 92a-93a. The Department's counterclaim was denied based upon the court's conclusions that private funds received by SLFI from a private source did not constitute reserve funds subject to a Federal interest and that all funds held by SLFI subject to a Federal interest determined pursuant to the applicable regulations had been totally and properly expended on program expenses. App. D, E at 44a-50a, 84a-85a.

The District Court amended its Decision and Judgment on February 7, 2000, by requiring SLFI to hold that portion of the judgment relating to future reinsurance claims in a separate fund and to return any such funds which remain after the loans guaranteed by SLFI are no longer outstanding. App. D at 32a-55a. The District Court's rulings on the interpretation of the contracts and the amount of damages were unchanged.

D. The Ninth Circuit Court of Appeals Decision

The Department appealed the decision of the District Court arguing that SLFI may not continue operations as to

obligations in place at the time of termination when it has terminated its agreements with the Secretary as to new loans. The Department claimed that the District Court further erred in determining that 1) the Department's counterclaim is moot and 2) SLFI holds no Federal funds or assets. SLFI appealed the portion of the District Court's amended opinion requiring SLFI to hold the award for future damages in a separate account with remaining funds, if any, to be returned to the Department since such issue was not raised at trial.

The Ninth Circuit rendered its opinion on December 4, 2001 holding that since the contractual provisions at issue are ambiguous the provisions were to be interpreted in light of the HEA and regulations and also by affording a "fair measure of deference" to the Secretary's interpretations. Deferring to the Secretary's interpretation of the contractual provisions, the Court posits that guaranty agencies are essentially creatures of regulatory agreements and federal regulations and "in light of the Act and regulations, SLFI was required by the termination clause in the agreements entered between itself and the Secretary to bow to the Secretary's directives once SLFI had terminated the agreements." App. B at 21a-22a.

The Ninth Circuit held that the District Court erred by interpreting the contractual provisions to provide for obligations which survive termination. The Court of Appeals reasons that if the Secretary had terminated "for cause" then "the Secretary's authority to control the functions of SLFI would have been absolute"; therefore, when SLFI voluntarily terminated the agreements SLFI was "required to cede decision-making control to the Secretary . . ." App. B at 13a, 18a.

The Ninth Circuit also held that the District Court erred in determining that the Secretary's position for defining

guaranty agency reserve funds which are subject to the Secretary's control is "contrary to clear congressional intent . . ." The Court of Appeals held that Congress has not defined "guaranty agency reserve funds" and then it accords *Chevron* deference to an interpretation of regulations which the Department argues defines guaranty agency reserve funds for purposes of the HEA. App. B at 23a-31a. SLFI's Petition for Rehearing and Rehearing En Banc was denied on April 15, 2002.[3] App. A at 2a.

REASONS FOR GRANTING THE PETITION

I. Common-law rules of contract construction, including the longstanding rule of *contra proferentem*, apply to government-drawn contracts.

A. The Ninth Circuit opinion contradicts the longstanding position of the Supreme Court on the interpretation of government contracts with private parties.

Interpreting the contractual provisions with respect to termination, which it held to be ambiguous, the Ninth Circuit applied a new rule by paraphrasing *Peterson v. United States Department of Interior*, 899 F.2d. 799, 807 (9th Cir. 1990), to resolve ambiguities purportedly by interpreting the contracts "against the backdrop of the legislative scheme." App. B at

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[3] Congress recognized that any delay in the payment of reinsurance could have detrimental effects upon a guarantor's solvency. *See* H.Rep. No. 99-383, 99th Congress 2nd Sess. vol. 4, 38-39 (1986) *reprinted in* 1986 U.S.S.C.A.N. 2609-10. SLFI has now been paying default claims without reinsurance for over seven years during the pendency of this matter. Review of the Ninth Circuit's opinion by the Supreme Court is requested in an effort to minimize unrecoverable consequential damages.

15a.[4] However, the relevant portions of *Peterson* (and of *F.H.A. v. The Darlington, Inc.*, 358 U.S. 84, 79 S.Ct. 141, 3 L.Ed.2d 132 (1958) cited by *Peterson*) consider whether certain absent, *not ambiguous*, provisions in a contract might be *implied*. Ignoring this fundamental distinction between ambiguous terms and implied terms, the Ninth Circuit upheld, under the authority of *Peterson*, the Secretary's interpretation of the ambiguous contractual terms without respect to common notions of contract interpretation and construction. And, although claiming to rely on *Peterson*, the Ninth Circuit ignores the legislative scheme implementing the contracts, as expanded by the amendments to the HEA in 1976, which was to induce private nonprofit and State entities to help the Federal government reduce problems in the faltering Federal student loan program. The Ninth Circuit's opinion would have been completely different if it had applied the rules for contract interpretation and construction used and adopted by the Supreme Court in cases involving contracts between private parties and the government.

In *Lynch v. United States*, 292 U.S. 571, 54 S.Ct. 840, 78 L.Ed. 1434 (1934), the Supreme Court ruled that:

> "Valid contracts are property, whether the obligor be a private individual, a municipality, a state, or the United States. Rights against the United States arising out of a contract with it are protected by the Fifth Amendment.

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[4] The Ninth Circuit notes that SLFI had to agree to contract with the Secretary "and submit to extensive federal regulation. 20 U.S.C. §1085(j)." App. B at 15a. Section 1085(j) defines "guaranty agency" as an entity which has an agreement with the Secretary. It does not mention federal regulation, extensive or otherwise.

> [citations omitted]. When the United States enters into contract relations, its rights and duties therein are governed generally by the law applicable to contracts between private individuals." (Emphasis added), *Id.* 292 U.S. at 579.

In *Perry* (citing to *Lynch* and the Sinking Fund Cases), emphasizing the point that the government is as much bound by their contracts as are individuals, and the government "incurs responsibilities similar to those of individuals who are parties to [contracts]," the Supreme Court stated, "Punctilious fulfillment of contractual obligations is essential to the maintenance of the credit of public as well as private debtors." *Perry v. United States*, 294 U.S. 330, 55 S.Ct. 432, 79 L.Ed. 912 (1935). The plurality and concurring opinions in *Winstar* restate the Supreme Court's firm resolve to evaluate contracts between the government and private parties by applying "ordinary principles of contract construction and breach that would be applicable to any contract action between private parties." *Winstar*, 35 L.Ed.2d plurality opinion at 988, opinion of J. Breyer at 1013-1015, opinion of J. Scalia at 1019 (this issue was not addressed by the dissent). The Supreme Court must necessarily overrule this fundamental principle of contract construction if lets the Ninth Circuit's opinion stand.

The Supreme Court has recognized and implemented the common law rule of contract interpretation that ambiguous contractual language should be construed against the party that drafted it. *See Mastrobuono v. Shearson Lehman Hutton, Inc., et al.*, 514 U.S. 52, 115 S.Ct. 1212, 131 L.Ed.2d 76 (1995). Pursuant to *Lynch*, *Perry*, *Winstar*, etc., it is clear that this common law rule of contract interpretation applicable to contracts between private parties is equally applicable in

cases involving government contracts with private parties. Consistent with *Mastrobuono*, the Supreme Court has applied this rule against the government as the drafter of contracts in the case of *United States v. Seckinger*, 297 U.S. 203, 210, 90 S.Ct. 880, 25 L.Ed.2d 224 (1970). In *Seckinger*, as relied upon by the District Court, the Supreme Court unequivocally upholds (in both the majority and dissenting opinions) "the general maxim that a contract should be construed most strongly against the drafter, which in this case was the United States." *Id.* 397 U.S. at 208. Further, "as between two reasonable and practical constructions of an ambiguous contractual provision . . . the provision should be construed less favorably to that party which selected the contractual language. This principle is appropriately accorded considerable emphasis in this case because of the Government's vast economic resources and stronger bargaining position in contract negotiations." *Id.* 397 U.S. at 216-17.

The Ninth Circuit opinion refuses to apply this common law rule (or any common rules of contract construction) and instead opts for interpretations of the contractual provisions at issue which are not readily apparent from their plain language. In fact the interpretations adopted by the Ninth Circuit were only first proposed by Department representatives in the context of this litigation and are reached only through a convoluted construction of HEA provisions (specifically, §1078(c)(9)(E) & (F) which the Department repeatedly stated are not applicable to this case). App. B at 17a-21a. Indeed, the Ninth Circuit's interpretation seemingly adopts the government's argument made at trial that the contracts are illusory.

This conflict between the Ninth Circuit's rule for interpreting government contracts, which it used to the exclusion of general rules of contract construction, cannot be

reconciled with the Supreme Court's holdings that rules of contract interpretation applicable to private contracts (specifically, the rules of *contra proferentem* and giving the language used its plain and ordinary meaning) are applicable to government contracts with private parties.[5]

B. The Ninth Circuit's opinion contradicts the opinions of the Court of Appeals for the Federal Circuit on how to construe and interpret the government's contracts with private parties.

Consistent with the Supreme Court opinions cited above, the Federal Circuit applies the rule of *contra*

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[5] The Ninth Circuit's opinion also conflicts with the language of the HEA authorizing the Secretary to enter into reinsurance agreements with guaranty agencies. The authorizing statute provides that ". . . The guaranty agency shall, be deemed to have a contractual right against the United States, during the life of such loan . . ." (Emphasis added) 20 U.S.C. §1078(c)(1)(A). The Ninth Circuit dismisses this statutory language by holding that the contractual obligation runs with the loan purportedly in order to harmonize the provision with the Secretary's ability "to require the transfer of loans from a guaranty agency under certain conditions" (App. B at 21a) while ignoring the fact as demonstrated at trial and conceded by the Department that no such conditions exist; and further ignoring that even if the Secretary's position prevailed the only party legally implicated on the loan guarantees is SLFI and SLFI has paid and continues to pay all valid claims as demonstrated at trial. The bilateral nature of the obligations (i.e., the honoring of guarantees by SLFI and the reimbursement by the Secretary) are analogous to the rights and obligations of the mortgagors and the agency in *Franconia Associates v. United States*, 536 U.S. ____, No. 01-455, Slip Opinion (June 10, 2002), absent which the agreements are illusory.

proferentem in resolving ambiguities in government-drawn contracts. In applying this rule, the Federal Circuit has held that latent ambiguities in government contracts are to be construed against the government as drafter. *See Hunt Construction Group v. United States*, 281 F.3d 1369 (Fed. Cir. 2002)(holding when ambiguity in a government contract is latent, court is to construe the ambiguous term against the government as drafter of the contract, provided the contractor's interpretation is reasonable and the contractor relied on that interpretation); *P.R. Burke Corp. v. United States*, 277 F.3d 1346 (Fed. Cir. 2002); *Metric Constructors, Inc. v. National Aeronautics and Space Admin.*, 169 F.3d 747 (Fed. Cir. 1999); *see also*, *Lockhead Martin IR Imaging Systems, Inc. v. West*, 108 F.3d 319 (Fed. Cir. 1997)(". . . if there is no facial ambiguity, criterion is whether contractor reasonably interpreted contract, applying usual rule of *contra proferentem* against the contract draftor . . . if some substantive provision of government-drawn agreement is fairly susceptible of certain construction and contractor actually and reasonably so construes it, in course of bidding or performance, that interpretation will be adopted."); *H.B. Mac, Inc. v. United States*, 153 F.3d 1338 (Fed. Cir. 1998)(holding that court is to place itself into shoes of reasonable and prudent contractor, and decide how such a contractor would act in interpreting contract documents). The Court of Claims has gone further and determined in cases of ambiguity, the contractor's interpretation may prevail over the government's even though the government's interpretation may be more reasonable, since the government drafted the contract. *See Nielsen-Dillingham Builders v. United States*, 43 Fed.Cl. 5 (1999).

In the present case, the Ninth Circuit opinion does not apply the rule of *contra proferentem* or any other general rule of contract construction to resolve what it calls "ambiguous"

contractual provisions. The contract ambiguity rule the Ninth Circuit should have applied is that enunciated by the Federal Circuit (and Supreme Court) in the case law cited above. This conflict between the Ninth Circuit and the Federal Circuit on how to construe and interpret government-drawn contracts cannot be reconciled and necessitates review by the Supreme Court.

II. A government agency's informal and inconsistent interpretation of its own regulations is not entitled to *Chevron* deference.

"The Secretary has express authority to promulgate regulations under the [HEA]. 20 U.S.C. §1082(a)(1). In analyzing the regulations governing a guaranty agency's reserve funds, we therefore apply the framework outlined in Chevron U.S.A., Inc. v. Natural Res. Def. Council, Inc." App. B at 23a. After citing these general rules, the Ninth Circuit, citing *United States v. Mead Corp.*, ___ U.S. ___, 121 S.Ct. 2164, 150 L.Ed. 292 (2001), states "When Congress has explicitly left a gap for an agency to fill, there is an express delegation of authority to the agency to elucidate a specific provision of the statute by regulation, and any ensuing regulation is binding in the courts unless manifestly contrary to the statute." App B at 23a.

The statutory provision at issue is 20 U.S.C. §1072(g)(1) enacted in 1993. The regulation to which the Ninth Circuit gives deference as defining "reserve funds" for purposes of §1072(g)(1) is 34 C.F.R. 682.410(a)(1) promulgated by the Secretary in 1986.[6] App. H at 108a-110a.

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[6] In adopting such regulations, the Secretary responded to questions as to whether gifts or grants received for a specific purpose should be included as part of the reserve. In response the

According *Chevron* deference, the Ninth Circuit holds that Congress by its silence intended for this pre-existing regulation (682.410(a)(1)) to define "reserve funds" for purposes of §1072(g)(1) whereas if Congress had "intended to narrow the regulatory scope of reserve funds it would have done so explicitly." App. B at 24a-27a. This reasoning contradicts the rule set forth in *Mead* which allows the Secretary to fill gaps in the statute through the promulgation of "ensuing regulations" and wrongfully gives *Chevron* deference to an informal interpretation of this pre-existing regulation.[7] This conclusion conflicts, as found by the District Court, with the clear intentions of Congress and also conflicts with the prior statements and positions of the Secretary.

"[A]dministrative implementation of a particular statutory provision qualifies for *Chevron* deference when it appears that Congress delegated authority to the agency

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Secretary stated: "The Secretary believes that *all funds generated as a result of a guarantee agency's administration of its loan guarantee program* should be reserved for use by that guarantee agency in performing its duties as a guarantee agency." (Emphasis added). Fed. Reg. vol. 51, No. 217, Monday, Nov. 10, 1986, p. 40943. SLFI and Department witnesses established at trial that the funds found by the District Court to be "non-Federal" were not "generated as a result of [SLFI's] administration of its loan guarantee program."

[7] Deference should clearly not be given in instances when the administrative agency admits it does not understand the statute. *See* Fed. Reg. vol. 59, No. 226, Friday, Nov. 25, 1994, Rules and Regulations, p.60689, "Section 682.410(a)(1) Reserve Fund Assets." The Secretary in declining to define non-Federal portion does so based on a lack of understanding of what "Federal portion" means.

generally to make rules carrying the force of law, and that the agency interpretation claiming deference was promulgated in exercise of that authority." *Mead*, 121 S.Ct. at 2171. Here, the Secretary's interpretation of the regulation, namely, that 34 C.F.R. 682.410(a) defines reserve funds for purposes of §1072(g)(1), is not an interpretation of §1072(g)(1) promulgated under the Secretary's rulemaking authority; but rather, an informal interpretation of a pre-existing regulation made by counsel in the context of this litigation. The application of *Chevron* deference to such an informal regulatory interpretation is in direct conflict with *Mead*.

In 1992, upon the conclusion of the so-called "spend down" litigation, Congress amended §1072(a)(2) by adding "Except as provided in section [1078](c)(10)(E) or (F), such unencumbered non-Federal portion shall not be subject to recall, repayment, or recovery by the Secretary." App. H at 100a-101a. Consistent with this amendment Congress stated that ". . . the unencumbered non-Federal portion of a guaranty agency's reserve fund shall not be subject to spend down." H.Conf.Rep. No. 102-630, 102nd Cong. 2nd Sess. vol. 4, 451 (1992) *reprinted in* 1992 U.S.C.C.A.N. 566. App. I at 119a. Then in 1993 Congress enacted §1072(g)(1) and stated that ". . . all references to guaranty agency reserves contained in amendments to [§1072] refer only to the "Federal portion" of such reserves."[8] H.Conf. Rep. No. 103-

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[8] The Ninth Circuit observes ". . . ascertaining congressional intent from Congress's failure to act is a difficult proposition . . ." (App. B at 26a) while ignoring that in enacting §1072(g)(1) Congress did act to require standards with respect to the return of a portion of a guaranty agency's reserve fund, or any reserve funds or assets, be developed through negotiated rulemaking. It was such negotiated rulemaking which attempted to develop "a better definition of reserve fund." See Fed. Reg. vol.

213, 103rd Cong. 1st Sess. vol. 3, 456 (1993) *reprinted in* 1993 U.S.C.C.A.N. 1145. App. I at 119a-120a. The Secretary's position that section 682.410(a) defines reserve funds for purposes of §1072(g)(1) is not entitled to deference, let alone *Chevron* deference, because it is manifestly contrary to the clear intent of Congress that certain guaranty agency funds, which under the regulations might be included in reserve funds, are non-Federal property under §1072(a)(2).

In addition, the Ninth Circuit ignored the Secretary's admission that the statute (§1072(a)(2)) supersedes the regulation (682.410(a)). After enactment of the amendment to §1072(a)(2) referenced above, Secretary acknowledged,

> "The final regulations incorporate statutory changes . . . to reflect self-implementing provisions of the Higher Education Amendments of 1992 (1992 Amendments)(enacted July 23, 1992). To the extent these regulations may be inconsistent with the 1992 Amendments, the 1992 Amendments supersede the regulations. The remainder of the provisions enacted as part of the 1992 Amendments will be addressed in separate proposed and final regulations developed under the requirements of negotiated rulemaking." Fed. Reg. vol. 57, No. 244, Friday, Dec. 18, 1992, p. 60280.[9]

59, no. 153, *supra*.

[9] The result of negotiated rulemaking, including an attempt to provide a better definition of the reserve fund under 682.410(a), was not evidenced by proposed rules until well after SLFI's termination of July 1, 1994. See Fed. Reg. vol. 59, no. 153, Wednesday, Aug. 10, 1994, proposed rules, p. 41184.

Thus to the extent section 682.410(a), or the Secretary's interpretation of such, conflicts with §1072(a)(2), which provides for the existence of non-Federal reserve funds and a formula for calculating such non-Federal funds, the statute supersedes the regulation. The Secretary's current position is exactly the opposite, namely, that the regulation, or the Secretary's interpretation of such,[10] supersedes the statute and Congress' specifically stated concurrent intent.

The Ninth Circuit opinion ignores the Secretary's prior statements concerning the Federal interest in guaranty agency reserve funds. Prior to this litigation, the only position expressed by the Secretary was that once a guaranty agency returns the Federal advances it received pursuant to 20 U.S.C. §1072(a) and/or §1072(c) then the guaranty agency's reserves are no longer restricted by the Federal regulations and there is no longer a Federal interest in the guaranty agency's reserve funds.[11] *See* GAO Report, Aug. 1986, "Guidelines for

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[10] "The district court held that the Secretary's position, that all funds received by SLFI while acting as a guaranty agency, regardless of their origin, are federal reserve fund assets, was inconsistent with Congressional intent and the underlying purposes of the HEA . . ." App. A at 2a. "Yet, based upon the regulatory definition, and the position asserted by the Department in this instant action, any non-federal assets credited to a guaranty agency's reserve fund would be deemed a [federal] reserve fund asset . . ." App. E at 79a.

[11] The attributes of control and extensive regulation of guaranty agencies referred to in the spend down cases arise out of the agreements with respect to advances made pursuant to 20 U.S.C. §1072(a) and the related regulations. Both parties acknowledge that SLFI never sought nor received such §1072(a) advances. App. B at 29a-30a.

Reducing Guaranty Agency Reserves" p. 41[12] (this prior position was confirmed by the deposition testimony submitted at trial of former Assistant Secretary of the Department C. Ronald Kimberling).[13] App. L at 141a. Section 682.410(a) was in place during the prior and present positions of the Secretary. These conflicts between the Secretary's positions emphasizes the error in granting *Chevron* deference to the Secretary. *See Good Samaritan Hospital v. Shalala*, 508 U.S. 402, 113 S.Ct. 2151, 124 L.Ed.2d. 368 (1993)(holding that an agency's interpretation of a relevant provision which conflicts with the agency's earlier interpretation is entitled to considerably less deference).

Other rules of statutory construction in conflict with the Ninth Circuit opinion include:

1. "[A] statute ought, upon the whole, to be so construed that, if it can be prevented, no clause, sentence, or word shall be superfluous, void, or insignificant." *Duncan v. Walker*, ___ U.S. ___, 121 S.Ct. 2120, 2125, 150 L.Ed.2d 251 (2001). The Ninth Circuit opinion renders other provisions of the HEA meaningless further showing why

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[12] In enacting former 20 U.S.C. §1072(e) as part of P.L. 100-203 which gave rise to the so-called "spend down" litigation, the Congress noted its lack of confidence in the Department's regulations by (i) providing a definition of "cash reserves" and related definitions (101 STAT 1330-38) and (ii) in the Conference Report citing to the GAO guidelines referenced above. App. H at 101a-102a.

[13] It should be noted that under the Secretary's prior formalized position, (i.e., the Federal portion of guaranty agency reserves consisted of Federal advances and earnings on the advances) all statutes at issue in this case can be read to be consistent.

Chevron deference is wrong. For example:

• Under the Ninth Circuit's opinion there could never be such thing as an "unencumbered non-Federal portion of a guaranty agencies reserve funds," although in §1072(a)(2) Congress identified such and provided a formula for calculating such "unencumbered non-Federal portion."

• Section 1078(c)(6) provides that a guaranty agency may retain a portion of collections while the remainder is remitted to the Department as the "Secretary's Equitable Share." The regulations require that 100% of collections be credited to the reserve fund. Thus, under Ninth Circuit's opinion the portion not remitted to the Secretary and the portion remitted to the Secretary are both Federal property and the provision for the "Secretary's Equitable Share" is void of meaning.

• In 1993, Congress amended §1078(c)(1) to reduce reinsurance rates on new loans to 78%, 88% or 98% depending on the guaranty agency's default rates. This reduction was part of Congress' effort to increase "risk sharing" among participants in the Federal Family Education Loan Programs. "Risk sharing" and the reduction in reinsurance rates have no meaning under the Ninth Circuit's opinion which creates a situation of just moving Federal money from one pocket to another.

• Under the Ninth Circuit's opinion guaranty agencies are mere servants of the Federal government; therefore, there is no need for the Secretary to invoke the procedures of §1072(g)(1) or §1078(c)(9)(E) & (F) to acquire control of an insolvent (or even solvent) guaranty agency's reserve funds and assets. Such opinion renders meaningless the procedural safeguards in §1072(g)(1) and §1078(c)(9)(E) & (F).

2. "[W]hen two statutes are capable of co-existence . . . it is the duty of the courts, absent a clearly expressed congressional intention to the contrary, to regard each as effective." *Vimar Seguros v. M/V Sky Reefer*, 515 U.S. 528, 115 S.Ct. 2322, 132 L.Ed.2d 462 (1995); *see also*, *Watt v. Alaska*, 451 U.S. 259, 101 S.Ct. 1673, 68 L.Ed. 80 (1981)(applying maxim that repeal by implication is not favored). The Ninth Circuit's opinion would repeal §1072(a)(2) by implication asserting that by using the "notwithstanding" term in §1072(g)(1) Congress intended to supersede portions of §1072(a)(2) which were enacted only one year earlier. This result ignores clear concurrent statements of congressional intent and construes the statutory provisions in such a way as to create a conflict. As discussed above, rather than repeal §1072(a)(2) by implication, the statutory provisions at issue can and should be read to be consistent and in a manner so that they are not meaningless or superfluous.

3. In *United States v. Shreveport Grain & Elevator Co.*, 287 U.S. 77, 53 S.Ct. 42, 77 L.Ed. 175 (1932), the Supreme Court ruled that a statutory construction which avoids the doubt which might otherwise arise as to the constitutionality of a statute is to be adopted if reasonably possible. *See also Edward J. DeBartolo Corp. v. Florida Gulf Coast Building & Constr. Trades Council*, 485 U.S. 568, 575, 108 S.Ct. 1392, 99 L.Ed.2d. 645 (1988). The Ninth Circuit's construction, and deference to the Secretary's construction, of §1072(g)(1) and §1078(c)(1)(A) raises significant constitutionality questions when such provisions are used to take away a guaranty agency's contractual right to reimbursement and to federalize private funds and assets.[14]

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[14] The Ninth Circuit asserts that SLFI's and the District Court's reading of 20 U.S.C. §1078(c)(1)(A) to provide a

These constitutionality problems are avoided by construing the statutes and contracts, as done by the District Court, to protect SLFI's contractual right to reimbursement and by allowing private funds received by a guaranty agency from a private source to retain their non-Federal character.

Based on the above-noted inconsistencies and conflicts, little, if any, deference should be granted to the Secretary. The Ninth Circuit should have applied the rules of statutory construction cited above and construed the provisions consistent with each other and with the purposes of the HEA.

III. The Opinion of the Ninth Circuit is Incorrect.

No private entity would dare enter into contracts with the Federal government if it could anticipate that fourteen years after the contracts are executed the government would, through statutory or regulatory enactment or otherwise (in the present case through a letter from a Department employee, App. N at 143a-146a), render the contracts to be merely "regulatory agreements" containing only illusory promises

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contractual right to reimbursement would abrogate the Secretary's right to require the assignment of loans under 20 U.S.C. §1078(c)(8), which the Ninth Circuit cites as: "if the Secretary determines that the protection of the Federal fiscal interest so requires, a guaranty agency shall assign to the Secretary any loan of which it is the holder . . ." App. B. at 20a. By using an ellipsis the Ninth Circuit obscures the statute and renders void the remainder of the statute which provides "and for which the Secretary has made a payment pursuant to paragraph (1) of this subsection." App. H at 105a. It is entirely consistent under the statute to provide (as argued by SLFI and concluded by the District Court) that the guaranty agency is entitled to reimbursement and that subsequent to such reimbursement by the Secretary, the Secretary might direct the transfer of the underlying loan.

and then, based on such "regulatory agreements" which provide no enforceable rights to the entity, attempt to federalize certain private funds and assets acquired by the private entity. Such a result is clearly contrary to the purposes of the HEA, specifically the 1976 Amendments, which were to encourage and induce State and private non-profit guaranty agencies to participate in the Federal student loan programs. Contrary to the Ninth Circuit's opinion, the purpose of the HEA was not to create "servants of the Federal government" whose private funds and assets, according to the Secretary, are merely extensions of the Federal treasury.

The HEA as revised in 1976 (P.L. 94-482) requires the U.S. Commissioner of Education to encourage the establishment of a State or private nonprofit student loan insurance program by each state. Congress enacted several financial incentives to encourage States and private nonprofit entities to participate, as noted above. The HEA and these amendments never contemplated, nor could it have been reasonably anticipated by either party when SLFI and the Secretary began this cooperative venture in 1978, the result that has been fashioned by the Ninth Circuit.

The termination provisions of the contracts as drafted by the Department state:

> "The Commissioner's obligations to make payments, as provided for in this Agreement, **shall extend only with respect to loans insured by the Agency prior to termination** of this agreement or prior to the expiration of the authority provided in the Act.
>
> "This Agreement may be terminated by either party upon not less that [sic] 60 days written notice to the other party, except that

> the Commissioner may terminate this Agreement only for cause. **Termination shall not affect obligations incurred under this Agreement by either party before the effective date of termination**. If termination is effected by the Commissioner, it will not become final until the Agency has been afforded reasonable notice and an opportunity for a hearing, except that the Commissioner may suspend this Agreement pending the outcome of the hearing if he determines that such action is necessary in order to prevent substantial harm to Federal interests." (Emphasis added). App. J at 125a; K at 133a-134a.

Using common notions of contract construction and interpretation the District Court found that these provisions allowed for contractual rights and obligations (of both parties) existing at the time of termination to survive termination. App. E at 67a-70a, 86a. To the contrary, purportedly using *Peterson* as authority, the Ninth Circuit interpreted these contractual provisions to mean that the Secretary's obligation to make payments does not extend to the Agency (i.e., SLFI), but is an obligation which runs only with the loan.[15] App. B

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[15] The Ninth Circuit's error is compounded by holding that the Secretary may transfer SLFI's loan guarantees without meeting the statutory requirements for directing such a transfer. App. B at 13a, 22a. The initial Ninth Circuit panel held that the Secretary's directives to SLFI did not satisfy the statutory requirements for directing such a transfer. However, in its final opinion, the Ninth Circuit concludes that it is unnecessary to look at the statutory requirements imposed on the Secretary's directives because SLFI is a mere "servant of the Federal government" obligated to "bow

at 21a. Further, the Ninth Circuit held that the statement "Termination shall not affect obligations incurred under this Agreement by either party before the effective date of termination" refers only to obligations incurred during a "wrap-up" period existing between the "date of termination" and the "effective date of termination."[16] App. B at 14a-21a.

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to the Secretary's directives." In addition to permitting the Secretary to avoid satisfying statutory requirements (i.e., "best interest determination" (§1072(g)(1)), "termination of operations" (§1072(g)(1)), approval from loan holder (§1078(b)(2)(E)), payment of reinsurance (§1078(c)(8)), and termination "for cause" (§1078(c)(9)(E))), the Ninth Circuit authorizes the Secretary to avoid the due process procedures mandated by the HEA.

[16] The Ninth Circuit gives some deference to the Secretary's assertion of a "wrap-up" period. App. B at 21a. The Ninth Circuit never indicates how this interpretation is that of the Secretary. It is not mentioned or alluded to in any regulation, bulletin, letter or utterance of the Secretary and is, most probably, the creation of the Justice Department attorney who first raised it at oral arguments before the earlier Ninth Circuit panel in 1996. Subsequent to such argument, the Department, in its "Memorandum of Law in Support of Defendant's Motion for Summary Judgment with Regard to Plaintiff's Second Amended Complaint" dated October 29, 1997, offers a different interpretation which did not provide for any "wrap-up" period: "The only obligations the government may have had would have related to insurance money not yet paid by [the Department] at the time of termination for guarantees on which SLFI had paid lenders before termination. All such obligations were paid by [the Department] long ago." At page 6.

This latter interpretation was also proffered post-trial by the Department in its "Proposed Findings of Fact, Conclusions of Law, Order and Judgment Submitted in Connection with October 19, 1998 Trial," dated December 8, 1998, at pages 33-34, item 56(c), and the "wrap-up" language did not re-appear until the referenced

These theories, specifically, that the Secretary's obligation extends only to the loan and not to the contracting private party and of a "wrap-up" period, were first proposed by the Department in the context of this litigation. Neither the HEA nor the Federal regulations provide for these theories or anything approximately thereto.[17]

Applying common rules of contract construction and interpretation to these contractual provisions it is reasonable and correct to conclude, as did the District Court, that 1) the Secretary's obligation to make payments under the agreement for loans insured by SLFI is an obligation to SLFI for loans

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Justice Department attorney rejoined the case before the Ninth Circuit.

[17] In the only court case with a similar factual basis to the present case (i.e., guaranty agency informed Secretary that it would not guaranty any new loans and agreements were terminated as to insuring new loans), the Secretary by his actions conceded that termination of the agreements did not affect obligations in place prior to termination, that obligations survived termination and that the Secretary's obligation to pay reinsurance was to the guarantor. *See Education Assistance Corp. v. Cavazos*, 902 F.2d 617 (8th Cir. 1990)(this case did not attempt to interpret the contracts, rather the court addressed the issue of whether a statutory provision authorizing the Secretary to recover excess reserves was constitutional). The Secretary affirmatively stated in *Education Assistance Corp.* that the Secretary would not reinsure any loans guaranteed by the guarantor ("EAC") on or after the date of termination. *Id.* 902 F.2d at 621. The facts found by the court then establish that the Secretary continued paying reinsurance to EAC for loans guaranteed by EAC prior to termination and nearly one year after termination of the agreements the Secretary began to recover "excess reserves" through an offset against payments then being made to EAC. *Id.*

insured by SLFI prior to termination of the agreements, and 2) termination of the agreements does not affect the Secretary's (or SLFI's) obligations in place at the time of termination which, after providing for the 60 day notice requirement and as stated in SLFI's notice to the Secretary, occurred on July 1, 1994.

It also could not have been anticipated that by entering into contracts with the Secretary certain private funds received by SLFI would be converted into Federal property. Indeed, no State or private nonprofit entity would have entered into contracts with the Secretary if such a federalizing of private property could have been anticipated. The District Court recognized that by SLFI's acceptance and use of certain private funds the non-Federal characteristic of such funds was not changed. To the contrary, the Ninth Circuit, by incorrectly applying *Chevron* deference to an informal interpretation of the regulations, makes it possible for the Secretary to argue that any private funds of the guaranty agencies are Federal property.[18] Such a conversion of private funds into Federal property contradicts the purposes of the HEA and, as noted above, the Secretary's current position on this issue is not entitled to deference.

CONCLUSION

The Student Loan Fund of Idaho, Inc. respectfully submits that this petition for writ of certiorari should be granted and the conflict between the decisions of the Ninth Circuit and the Supreme Court and Federal Circuit resolved. At a minimum, the Supreme Court should accept review and

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[18] SLFI does not concede that certain private funds accepted and used by SLFI fall within the regulatory definition of reserve funds.

direct that the rule of *contra proferentem* be applied here and that *Chevron* deference not be applied to the Secretary's informal and inconsistent interpretation of regulations.

RESPECTFULLY SUBMITTED,

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APPENDIX A

UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

Nos. 99-36035, 99-36078, 00-35310, 00-35524

[Filed April 15, 2002]

STUDENT LOAN FUND OF IDAHO, INC., Plaintiff-Counter-Claim-Defendant-Appellee-Cross-Appellant,	)
v.	)
U.S. DEPARTMENT OF EDUCATION, Defendant-Appellant- Cross-Appellee,	)
and	)
DR. RODERICK R. PAIGE,* in his official capacity as Secretary of the United States Department of Education, Defendant-Counter-Claimant-Plaintiff-Appellant-Cross-Appellee.	)

* Dr. Roderick R. Paige is substituted for his predecessor, Richard W. Riley, as Secretary of the United States Department of Education. Fed R. App. P. 43(c)(2).

JUDGES:
Before James R. Browning, J. Clifford Wallace, and Thomas G. Nelson, Circuit Judges.

OPINION

The slip opinion filed December 4, 2001, is hereby amended as follows:

Page 16395, first paragraph, line 15, delete "The district court held, however, that the regulations were contrary to Congress's intent and that these funds from a separate, private entity should not be considered part of the federal reserve fund." and replace it with "The district court held that the Secretary's position, that all funds received by SLFI while acting as a guaranty agency relating to its operations as a guaranty agency, regardless of their origin, are federal reserve fund assets, was inconsistent with Congressional intent and the underlying purposes of the HEA and that these funds from a separate, private entity should not be considered part of the federal reserve fund."

The panel has voted to deny the petition for rehearing. Judge T.G. Nelson has voted to deny the suggestion for rehearing en banc, and Judge Browning and Judge Wallace so recommend.

The petition for rehearing and the petition for rehearing en banc are DENIED.

APPENDIX B

UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

Nos. 99-36035, 99-36078, 00-35310, 00-35524

[Filed December 4, 2001]
[As Amended by the April 15, 2002 Order and Amended Opinion]

STUDENT LOAN FUND OF IDAHO, INC.,
Plaintiff-Counter-Claim-Defendant-Appellee-Cross-Appellant,

v.

U.S. DEPARTMENT OF EDUCATION,
Defendant-Appellant- Cross-Appellee,

and
DR. RODERICK R. PAIGE,* in his official capacity as Secretary of the United States Department of Education,
Defendant-Counter-Claimant-Plaintiff-Appellant-Cross-Appellee.

* Dr. Roderick R. Paige is substituted for his predecessor, Richard W. Riley, as Secretary of the United States Department of Education. Fed R. App. P. 43(c)(2).

Appeal From the United States District Court
for the District of Idaho
Larry M. Boyle, Magistrate Judge, Presiding
D.C. No. CV-94-00413-LMB

JUDGES:
Before James R. Browning, J. Clifford Wallace, and Thomas G. Nelson, Circuit Judges. Opinion by Judge Wallace.

OPINION

WALLACE, Circuit Judge:

In this appeal, we are asked to interpret a difficult contract and attempt to divine what the Congress meant in portions of the Higher Education Act (Act). The importance of the issues cannot be gainsaid, as they deal with loans to post-secondary students.

We suppose the complexity of the case is demonstrated by the fact that both parties appeal from the judgment of the district court. The Department of Education and Secretary of Education (together, Secretary) argue that the district court erred both in holding that the Secretary was in breach of his obligations to the Student Loan Fund of Idaho, Inc. (SLFI) and in interpreting the agreements entered between SLFI and the Secretary to allow the continuation of SLFI's guaranty operations even after SLFI terminated the agreements and ceased to guarantee new loans. In the alternative, the Secretary argues that even if SLFI had limited contractual authority to continue its operations, the Secretary has removed this authority by making a "best interest" determination. Finally, the Secretary argues that the district court failed to afford proper deference to the applicable regulations, promulgated pursuant to the Secretary's authority

under the Act, in determining the Secretary's rights in SLFI's reserve fund assets.

In its cross-appeal, SLFI argues that the district court erred in requiring SLFI to hold a large portion of the awarded damages in a separate account to be used solely for paying its future obligations on guarantee claims, with any excess to be returned to the Secretary. In addition, SLFI argues that the district court abused its discretion in denying SLFI's motion to amend its complaint to include Bivens claims. The district court had jurisdiction pursuant to 28 U.S.C. § 1331 and 20 U.S.C. § 1082(a)(2). We have jurisdiction of the timely filed appeal and cross-appeal pursuant to 28 U.S.C. § 1291. We reverse and remand.

I.

SLFI is a private non-profit corporation that began in the late 1970s to function as a guaranty agency under the Federal Family Education Loan Program (Loan Program), formerly known as the Guaranteed Student Loan Program. Under the Loan Program, private lenders provide financing to qualifying students attending post-secondary educational programs. The lenders enter into agreements with and pay insurance premiums to a guaranty agency which then guarantees repayment in case of default on the student loans. The ultimate insurer of the loans is, however, the federal government. 20 U.S.C. 1082(o). The Act, 20 U.S.C. §§ 1070, *et seq.*, and the regulations promulgated thereunder, 34 C.F.R. Part 682, govern the interaction between the federal government and the guaranty agencies.

The Act obligates the Secretary to provide reinsurance to the guaranty agencies during the life of the guaranteed loans. 20 U.S.C. § 1078(c)(1)(A). However, in order to become a guaranty agency within the meaning of the Loan Program and the Act, a State or private nonprofit organization is first required to contract with the Secretary. *See* 20 U.S.C. § 1085(j) (defining "guaranty agency" as "any State or nonprofit private institution or organization with which the Secretary has an agreement under section 1078(b) of this title."). At the time SLFI contracted with the Secretary (then Commissioner), the Secretary employed a series of standard regulatory agreements for bringing nonprofit entities into the Loan Program. *See, e.g., Colorado v. Cavazos*, 962 F.2d 968, 969 (10th Cir. 1992) (describing the series of contracts); *Educ. Assist. Corp. v. Cavazos*, 902 F.2d 617, 619 (8th Cir. 1990) (same). In large part, the provisions of the agreements either restate or implement the requirements of the regulations and the Act. Four of the five agreements entered into between SLFI and the Secretary provide that SLFI is to comply with the Act and the regulations promulgated thereunder. All of the agreements state that they are to be interpreted in the light of the Act and the regulations. Two of the agreements--the reinsurance agreement and supplemental reinsurance agreement--set the rates at which SLFI may obtain reinsurance from the Secretary. The reinsurance agreement provides that the Secretary will reimburse 80% of the amounts expended by SLFI in discharging its insurance obligations "with respect to loans insured by [SLFI] prior to termination of the agreement or prior to the expiration of the [reinsurance] authority in the Act." The supplemental reinsurance agreement provides that if the default rate is 5% or less, the Secretary will reimburse 100% of SLFI's expenses. If the default rate is more than 5% but does not

exceed 9%, then the Secretary reimburses 90% of expenses. These supplemental reinsurance rates apply only "with respect to loans insured by [SLFI] prior to the expiration of the [reinsurance] authority provided in the Act." These varying contractual rates of reinsurance track the rates then authorized by the regulations. *See* 34 C.F.R. § 682.404(a)(1) (1988); 34 C.F.R. § 682.405(a)(1) (1988).

The agreements, as well as the Act and regulations, require SLFI to maintain Loan Program funds in a "reserve fund." One of the agreements entered into between SLFI and the Secretary specifies that SLFI is required to deposit into a separate fund, called the Guarantee Fund by SLFI, (1) advances made by the Secretary (2) sums appropriated by the State for the purposes of the Loan Program, (3) money received as loan insurance premiums, (4) amounts "received by [SLFI] through gift, grant, or by other means from other sources" for Loan Program operations, (5) money collected on defaulted loans, and (6) interest or other earnings derived from the investment of the previously listed sources of money. The regulations require that funds from these same sources are to be included in the "reserve fund." 34 C.F.R. 682.410(a). The Act provides that the Secretary may require the return of the entire reserve fund of a guaranty agency only if "the Secretary [1] determines that such return is in the best interest of the operation of the program . . . or [2] to ensure [a] the proper maintenance of such agency's funds or assets or [b] the orderly termination of the guaranty agency's operations and the liquidation of its assets." 20 U.S.C. § 1072(g)(1).

The agreements between SLFI and the Secretary also provided for termination under certain circumstances with

results disputed by the parties. It is now undisputed that SLFI invoked this termination provision in April of 1994 and terminated its regulatory agreements effective as of July 1, 1994. In the Secretary's view, upon the termination of the regulatory agreements SLFI ceased to be a guaranty agency within the meaning of the Act and, as a result, was required to yield control over all of its guaranty functions to the Secretary. Here, the Secretary attempted to exercise such control by repeatedly ordering SLFI to end its guaranty operations and to transfer its entire loan portfolio and all of its reserve funds and assets (which in the Secretary's view constitute federal property) to a successor guaranty agency, the Northwest Education Loan Association (NELA).

SLFI refused, however, to comply with the Secretary's directives, asserting that the only effect on its operations of the termination of the agreements was that it could not guarantee new loans. With the exception of $81,841, SLFI has not transferred any reserve fund assets to the Secretary or NELA since June 30, 1994. The Secretary continued to reimburse SLFI until October 1994 at which time the Secretary instituted an offset against SLFI by withholding reimbursement payments. The Secretary suspended the offset during January and February of 1995 by making reimbursement payments in those months. However, since that time no other reimbursement payments have been made by the Secretary.

During September 1994, SLFI brought this action to challenge the legality of the Secretary's orders. The Secretary counterclaimed and, on a motion for summary judgment, ultimately obtained an injunction from the district court requiring SLFI to turn over all of its reserve fund. In the

same order granting the injunction, the district court granted SLFI's motion to amend its complaint to include a breach of contract claim. However, the district court denied SLFI's motion to include Bivens claims against the Secretary in his official capacity and three other Department of Education officials.

SLFI appealed from the injunction, and we reversed, holding in an unpublished disposition that there was still a genuine issue of material fact as to whether the Secretary had met the statutory requirements for requiring the return of all reserve funds. *Student Loan Fund of Idaho v. Riley*, No. 95-36179 (unpublished; table at 107 F.3d 17). SLFI also attempted to gain review of the district court's denial of its motion to amend its complaint to include Bivens claims. However, we held that at that stage of the case we lacked jurisdiction over that issue because SLFI's entire action had not been dismissed, and none of the relevant exceptions applied.

While the prior appeal before us was pending, the Secretary sought to remove any doubt as to whether SLFI had terminated its agreements and instituted its own "for cause" termination of the agreements pursuant to 20 U.S.C. § 1078(c)(9)(E). Had the Secretary succeeded in his efforts to effect such a termination, the applicable statutes would have provided the Secretary with plenary power over SLFI's operations. 20 U.S.C. § 1078(c)(9)(F). SLFI challenged the Secretary's termination notice in an administrative proceeding and at that point conceded through a stipulation that it had already terminated the agreements in 1994. The hearing officer ruled that he did not have jurisdiction to determine the validity of the Secretary's attempt to invoke his power to

terminate in light of SLFI's stipulation that the agreements were already terminated. In addition, following our prior decision in this case, the Secretary issued a "best interest" letter in an effort to meet one of the means specified in 20 U.S.C. § 1072(g)(1) for requiring the return of all of SLFI's reserve funds.

On remand from our court, the district court held a nine day trial on SLFI's breach of contract claim and determined that, as a matter of contract interpretation, SLFI had control upon termination of the agreements over whether to maintain its operations with respect to pre-termination loans. The district court agreed with the Secretary that SLFI is no longer a "guaranty agency" within the meaning of the Act, but it held that SLFI could continue operating as "a former guaranty agency, or private loan guarantor with existing obligations incurred under the [Loan Program]." One possible implication of this holding is that the Secretary cannot require the return of all SLFI's reserve fund assets on the basis that such return is necessary "to ensure . . . the orderly termination of the guaranty agency's operations and the liquidation of its assets," 20 U.S.C. § 1072(g)(1), because SLFI has elected not to terminate its operations.

The district court also held it unnecessary to reach the question of whether the Secretary could require the return of all reserve fund assets on the basis that the Secretary had "determined that such return [was] in the best interest of the operation of the program," *id.*, because the district court found that SLFI no longer had any federal reserve funds to return to the Secretary. The district court agreed with the Secretary that monies received from the Student Loan Fund of Idaho Marketing Association (IMA), which operates a

secondary market for student loans, would qualify under the regulations as reserve funds. IMA, because of its position in the secondary market for the loans, had a substantial interest in the operations of SLFI and infused capital – support fees and an additional $500,000 – into SLFI in order to support its guaranty operations. The district court held that the Secretary's position, that all funds received by SLFI while acting as a guaranty agency relating to its operations as a guaranty agency, regardless of their origin, are federal reserve fund assets, was inconsistent with Congressional intent and the underlying purposes of the HEA and that these funds from a separate, private entity should not be considered part of the federal reserve fund. In our prior opinion, the question of interpreting the termination provision of the agreements was not before us, and we expressly declined to reach the issue of to what extent the reserve fund could be deemed federal funds.

The district court determined that since SLFI was contractually authorized to continue its operations with respect to pre-termination loans, the Secretary was in breach of its reinsurance obligations to SLFI as to those loans. The court awarded $7,652,671 as reinsurance reimbursement for claims paid by SLFI with private money between November 1994 and March 1998. On appeal, the Secretary agrees that it owes reimbursement for this period since it would have had to pay reinsurance on the defaulted loans no matter who was insuring those loans; however, the Secretary disputes the amount. The court also awarded SLFI $8,502,832 as the present value of SLFI's projected insurance payments on its pre-termination loan portfolio for defaults occurring after March 1998. Finally, the court awarded SLFI $345,000 for damages based on lost business unrelated to SLFI's guaranty operations.

The Secretary filed a timely motion to amend the judgment pursuant to Federal Rule of Civil Procedure 59(e). The district court granted the motion in part and amended the judgment to require SLFI to put the $8,502,832 into an escrow account to be used only for paying the insurance claims of lenders, with any remainder to be returned to the Secretary. The district court reasoned that SLFI "could receive a windfall if for example future default rates fall below the historical default rates which [SLFI's] expert employed in calculating [SLFI's] future damages." If the default rate were to drop, "[SLFI] would have guaranty money left over . . . which rightfully belongs to the government."

II.

SLFI argues, and the district court held, that upon SLFI's termination of the agreements between itself and the Secretary, the decision whether SLFI would continue operations with respect to pre-termination loans devolved upon SLFI, not the Secretary. The Secretary argues that this holding is inconsistent with the terms of the agreements, particularly because the agreements are to be read in the light of the Act, the regulations, and legislative policy. The Secretary asserts that upon SLFI's termination of the agreements, SLFI became obligated to relinquish to the Secretary all decision-making control with respect to SLFI's guaranty functions under the federal program. Here, the Secretary decided that SLFI should cease all guaranty operations and, as part of the "orderly termination of the guaranty agency's operations," also required the return of all reserve funds. 20 U.S.C. § 1072(g)(1). Thus, in the Secretary's view, it is SLFI that is in breach of its duties to the Secretary.

The interpretation and meaning of contract provisions is a question of law that we review de novo. *See Mendler v. Winterland Prod. Ltd.*, 207 F.3d 1119, 1121 (9th Cir. 2000). We apply federal law in interpreting the contractual provisions at issue because an agency of the United States is a party to the contract. *See Mohave Valley Irrigation & Drainage Dist. v. Norton*, 244 F.3d 1164, 1165 (9th Cir. 2001). If we hold that SLFI was contractually required to cede decision-making control to the Secretary following the termination of its agreements with the Secretary, we will not need to reach the Secretary's alternative argument that it has made a best interest determination or the issues raised in SLFI's cross-appeal. We therefore discuss the Secretary's contractual argument first.

We begin with the language of the agreements which contains the following termination provision:

> This Agreement may be terminated by either party upon not less than 60 days written notice to the other party, except that the [Secretary] may terminate this Agreement only for cause. *Termination shall not affect obligations incurred under this Agreement by either party before the effective date of termination.* If termination is effected by the [Secretary], it will not become final until the Agency has been afforded reasonable notice and an opportunity for a hearing, except that the [Secretary] may suspend this Agreement pending the outcome of the hearing if he determines that such action is necessary in order to prevent substantial harm to the interests of the Federal Government.

(Emphasis added). SLFI argues that the language emphasized above means that termination of the agreement

does not alter obligations incurred before the termination. SLFI apparently reaches this result by equating the word "termination" with the phrase "effective date of termination" and positing that the prepositional phrase "before the effective date of termination" modifies the verb "incurred." According to SLFI, the implication of this interpretation is that SLFI may continue its operations essentially free of the Secretary's oversight and require the Secretary to provide reinsurance on pre-termination loans. Indeed, SLFI argues in its cross-appeal that the district court erred in exerting control over SLFI by requiring SLFI to hold the future damages award in a separate account to be used solely for the paying of defaulted loans, with any excess to be returned to the Secretary. Thus, SLFI asserts that its decision-making power over its present operations and funds should be virtually absolute now that it has withdrawn from its agreements with the Secretary.

The Secretary argues that the termination provision actually provides that obligations under the agreement are not altered until the termination is finalized, or "effective," at which time all obligations under the agreements cease. The Secretary refers to this as a "wrap-up" period. Thus, under this interpretation, the prepositional phrase "before the effective date of termination" would modify the verb "affect." The Secretary's interpretation is bolstered by the fact that the sentence immediately following the highlighted segment distinguishes between a termination and a final termination. According to the Secretary, once SLFI tendered its termination of the agreements, the Secretary had decision-making control as to how the wrap-up period would proceed and whether SLFI could continue limited operations thereafter.

Although we believe that the Secretary's reading is the more plausible of the two, the provision is not free from ambiguity. However, interpreting an ambiguous provision in a contract involving a federal agency is different from the same exercise when the contract involves private parties. In the instance before us, we attempt to resolve ambiguities by consulting the Act, the regulations, and the policies behind them. *Peterson v. United States Dept. of Interior*, 899 F.2d 799, 807 (9th Cir. 1990) (holding that governmental contracts must "be interpreted against the backdrop of the legislative scheme that authorized them, and our interpretation of ambiguous terms or implied covenants can only be made in light of the policies underlying the controlling legislation"). Indeed, in this case, we are required to do this by the agreements themselves.

First, SLFI was able to enter the Loan Program and receive the benefit of reinsurance only by agreeing to contract with the Secretary and submit to extensive federal regulation. 20 U.S.C. § 1085(j). Thus, guaranty agencies are essentially the creatures of regulatory agreements and federal regulations. As the Seventh Circuit has explained, "the guarantee agency . . . is heavily regulated by federal law. The purpose and legal structure of [a guaranty agency] places it in that borderline between the wholly public and wholly private instrumentality. The extensive federal regulation of the agency suggests its highly public nature." *Great Lakes Higher Educ. Corp. v. Cavazos*, 911 F.2d 10, 14-15 (7th Cir. 1990) (internal citation omitted). The court pointed out that "in essence [a guaranty agency] is an intermediary between the United States and the lender of the student loan. The United States is the loan guarantor of last resort. [The guaranty agency] assists the United States in performing that function."

Id. at 15. *See also Ohio Student Loan Comm'n v. Cavazos*, 900 F.2d 894, 899 (6th Cir. 1990) ("The [guaranty agency] is a public entity that is not interested in making any sort of profit in its administration of the [Loan Program]. Instead, it has chosen to join with the federal government to administer the [Loan Program] . . . .").

As the district court recognized, a guaranty agency without agreements with the Secretary is no longer a guaranty agency, but a "former guaranty agency, or private loan guarantor." While the district court did hold that SLFI remains under the "obligations imposed upon SLFI preparatory to receiving federal reimbursement," the district court provided no explanation as to how the Secretary is to exercise oversight over SLFI now that SLFI is no longer a party to any agreement with the Secretary. Further, SLFI now purports to operate largely outside the strictures of the Loan Program. This is emphasized by SLFI's contention that the district court erred in placing it under the obligation to use the damages award only to pay claims on defaulted student loans. Under the district court's decision, the federal government has thus lost its intermediary position between the lenders and itself with respect to the particular student loans guaranteed by SLFI prior to its having terminated its agreements. Yet the federal government remains the ultimate insurer of those loans, and the district court held that it must continue to pay reinsurance on those loans to SLFI, a "former guaranty agency or private loan guarantor," and not to NELA, the successor intermediary named by the Secretary and with whom the Secretary has Loan Program agreements.

This result is particularly striking when compared with the authority the Secretary would have had over SLFI if the

Secretary had terminated the agreements "for cause." 20 U.S.C. § 1078(c)(9)(E) provides a list of determinations the Secretary may make to effect the termination of its agreement with a guaranty agency:

> The Secretary may terminate a guaranty agency's agreement . . . if--
>
> > (i) a guaranty agency required to submit a management plan under this paragraph fails to submit a plan that is acceptable to the Secretary;
> >
> > (ii) the Secretary determines that a guaranty agency has failed to improve substantially its administrative and financial condition;
> >
> > (iii) the Secretary determines that the guaranty agency is in danger of financial collapse;
> >
> > (iv) the Secretary determines that such action is necessary to protect the Federal fiscal interest;
> >
> > (v) the Secretary determines that such action is necessary to ensure the continued availability of loans to student or parent borrowers; or
> >
> > (vi) the Secretary determines that such action is necessary to ensure an orderly transition from the loan programs under this part to the direct student loan programs under part D of this title.

The termination provision of the agreements provides that the Secretary may only terminate "for cause." Reading that contractual requirement in light of the Act, it becomes clear that the Secretary would have cause to terminate if any of the conditions in 20 U.S.C. § 1078(c)(9)(E) were met.

If before SLFI had terminated the agreements the Secretary had terminated the agreements "for cause"--that is, under the conditions prescribed by the Act--then the Secretary's authority to control the functions of SLFI would have been absolute. The Act commands, "If a guaranty agency's agreement under this subsection is terminated pursuant to [20 U.S.C. § 1078(c)(9)(E)] then the Secretary shall assume responsibility for all functions of the guaranty agency under the loan insurance program of such agency." 20 U.S.C. § 1078(c)(9)(F) (emphasis added). In carrying out this responsibility, the Secretary may:

> (i) permit the transfer of guarantees to another guaranty agency;
>
> (ii) revoke the reinsurance agreement of the guaranty agency at a specified date, so as to require the merger, consolidation, or termination of the guaranty agency;
>
> (iii) transfer guarantees to the Department of Education for the purpose of payment of such claims and process such claims using the claims standards of the guaranty agency, if such standards are determined by the Secretary to be in compliance with this chapter;

(iv) design and implement a plan to restore the guaranty agency's viability;

(v) provide the guaranty agency with additional advance funds . . . .

(vi) use all funds and assets of the guaranty agency to assist in the activities undertaken in accordance with this subparagraph and take appropriate action to require the return, to the guaranty agency or the Secretary, of any funds or assets provided by the guaranty agency, under contract or otherwise, to any person or organization; or

(vii) take any other action the Secretary determines necessary to ensure the continued availability of loans made under this part to residents of the State or States in which the guaranty agency did business, the full honoring of all guarantees issued by the guaranty agency prior to the Secretary's assumption of the functions of such agency, and the proper servicing of loans guaranteed by the guaranty agency prior to the Secretary's assumption of the functions of such agency, to avoid disruption of the student loan program, and to ensure an orderly transition from the loan programs under this part to the direct student loan programs under Part C of this subchapter.

Id. This list of powers clearly encompasses the directives issued by the Secretary in this case. However, as discussed above, the Secretary's attempt to invoke this provision was unavailing; an administrative hearing officer held that he was without jurisdiction to determine the validity of the Secretary's termination effort because the agreements had already been terminated by SLFI. Thus, SLFI's interpretation of the termination provision of the regulatory agreements allows a guaranty agency to circumvent the Secretary's power under 20 U.S.C. § 1078(c)(9)(F) by beating the Secretary to termination.

SLFI argues for its part that 20 U.S.C. § 1078(c)(1)(A) gives it the right to exact reinsurance from the Secretary. That provision states in part: "The guaranty agency shall be deemed to have a contractual right against the United States, during the life of such loan, to receive reimbursement . . . ." 20 U.S.C. § 1078(c)(1)(A). To read this provision as SLFI does would, however, abrogate the Secretary's right to transfer guarantees from a guaranty agency pursuant to 20 U.S.C. § 1078(c)(9)(F), discussed above. It would also abrogate its ability to require SLFI to assign loans to the Secretary pursuant to 20 U.S.C. § 1078(c)(8)(A), which provides, "If the Secretary determines that the protection of the Federal fiscal interest so requires, a guaranty agency shall assign to the Secretary any loan of which it is the holder ..." The Secretary suggests that the contractual obligation imposed is an obligation that runs with the loans. That is, if a loan is transferred to a different guaranty agency, the successor agency becomes "the guaranty agency" to which the Secretary is obligated to pay reinsurance under the statute. This interpretation harmonizes the various statutory provisions allowing the Secretary to require the transfer of loans from a

guaranty agency under certain conditions. The persuasiveness of the Secretary's position and the Secretary's expertise and long experience with the Loan Program leads us to accord a "fair measure of deference" to this interpretation. *See United States v. Mead Corp.*, 533, U.S. 218, 150 L. Ed. 2d 292, 121 S. Ct. 2164, 2171 (2001), citing *Skidmore v. Swift & Co.*, 323 U.S. 134, 139-40, 89 L. Ed. 124, 65 S. Ct. 161 (1944).

In addition, the Secretary's position is consistent with the language of the agreements it entered with SLFI. The reinsurance agreement provides: "The [Secretary]'s obligations to make payments, as provided for in this Agreement, shall extend only with respect to loans insured by the Agency prior to termination of this agreement or prior to the expiration of the [reinsurance] authority in the Act." The supplemental reinsurance agreement is similar: "The [Secretary's] obligation to make payments, as provided for in this Agreement, shall extend only with respect to loans insured by the Agency prior to the expiration of the [reinsurance] authority provided in the Act." In both cases, the obligations extend "with respect to loans" insured by SLFI and not with respect to SLFI. Nothing in these provisions indicate an intent on the part of the Secretary to give up his statutory authority to require SLFI to transfer its loan guarantees under certain conditions. Further, SLFI was on notice that it was subject to the regulations and the Act, and that the violation of such could give the Secretary cause to terminate the agreements and assume responsibility over SLFI's guaranty functions.

We hold that in light of the Act and the regulations, SLFI was required by the termination clause in the

agreements entered between itself and the Secretary to bow to the Secretary's directives once SLFI had terminated its agreements. To hold otherwise would be to give guaranty agencies, the servants of the federal government and of the public, the power to operate outside the Loan Program while still enjoying the benefits thereof. Therefore, the district court erred in holding that the Secretary breached its obligations to SLFI when SLFI had first breached its duties to the Secretary by continuing its guaranty operations without an agreement with the Secretary and in the face of clear directives to cease such operations. Because of this holding, it is unnecessary for us to discuss the Secretary's alternative "best interests" contention.

III.

However, one issue remains which we must address. The Secretary also argues that the district court should have included the support fees and $ 500,000 received by SLFI from IMA in calculating the amount in SLFI's "reserve fund."

The district court held, and the parties do not dispute, that these monies fall within the regulatory definition of reserve fund assets. Thus, the only question before us is whether the district court correctly determined that the regulations are contrary to clear congressional intent and thus should not control. We answer this question because, although the Secretary has agreed that it is liable for reinsurance for the loans defaulting during the period between November 1994 and March 1998, the amount calculated by the district court may be incorrect as a result of its error in defining the scope of federal ownership in SLFI's funds and assets. Whether the

district court properly interpreted federal statutes and regulations is a question of law we review de novo. *Tierney v. Kupers*, 128 F.3d 1310, 1311(9th Cir. 1997).

The Secretary has express authority to promulgate regulations under the Act. 20 U.S.C. § 1082(a)(1). In analyzing the regulations governing a guaranty agency's reserve funds, we therefore apply the framework outlined in *Chevron U.S.A., Inc. v. Natural Res. Def. Council, Inc.*, 467 U.S. 837, 843-44, 81 L. Ed. 2d 694, 104 S. Ct. 2778 (1984). *See* Mead Corp., U.S., 121 S. Ct. at 2171 ("When Congress has explicitly left a gap for an agency to fill, there is an express delegation of authority to the agency to elucidate a specific provision of the statute by regulation, and any ensuing regulation is binding in the courts unless . . . manifestly contrary to the statute." (internal quotation marks omitted)). Under this framework, we first must determine "whether Congress has directly spoken to the precise question at issue." *Rucker v. Davis*, 237 F.3d 1113, 1119 (9th Cir. 2001) (*en banc*). To make this determination, "we employ the traditional tools of statutory construction; if Congress had an intent on this issue, that intent is the law and must be given effect." *Id.* These tools of construction require us first to engage in a textual analysis of the relevant statutory provisions and to read the words of a statute "in their context and with a view to their place in the overall statutory scheme." *Id.* (internal quotation marks omitted). If the proper interpretation is not clear from this textual analysis, "the legislative history offers valuable guidance and insight into Congressional intent." *Id.* However, "it is well established that legislative history which does not demonstrate a clear and certain congressional intent cannot form the basis for enjoining regulations." *Rust v. Sullivan*, 500 U.S. 173, 189-

90, 114 L. Ed. 2d 233, 111 S. Ct. 1759 (1991).

The Secretary relies on 20 U.S.C. § 1072(g)(1) to establish that Congress has evinced an intent to allow the regulatory definition of "reserve fund" to control. Last amended in 1993, 20 U.S.C. 1072(g)(1) provides: "Notwithstanding any other provision of law, the reserve funds of the guaranty agencies, and any assets purchased with such reserve funds, regardless of who holds or controls the reserves or assets, shall be considered to be the property of the United States . . . ." 20 U.S.C. § 1072(g)(1). As has been previously discussed, this provision also provides that "the return of all reserve funds of a guaranty agency" may only be required if [1] a best interest determination is made by the Secretary or "[2] to ensure [a] the proper maintenance of such agency's funds . . . or [b] the orderly termination of the guaranty agency's operations." *Id.* The plain import of this provision is that "reserve funds" belong to the federal government, and such reserve funds may be recalled in their entirety under certain conditions. In addition, the "notwithstanding any other provision of law" clause demonstrates that Congress intended to supersede any previously enacted conflicting provisions. *See Cisneros v. Alpine Ridge Group*, 508 U.S. 10, 18, 123 L. Ed. 2d 572, 113 S. Ct. 1898 (1993). This provision does not, however, provide a congressional definition for "reserve funds of a guaranty agency." Indeed, the Act nowhere defines the term "reserve funds."

The Secretary would have us infer from the absence of such a definition an intent on the part of Congress to allow the regulatory definition to control. The Secretary argues from two sources of evidence that had Congress intended to

narrow the regulatory scope of "reserve funds" it would have done so explicitly. First, when 20 U.S.C. § 1072(g)(1) was amended in 1993, the regulations broadly defining such reserve funds were already well-established. *See* 57 Fed. Reg. 60, 354-55 (Dec. 18, 1992); *Educ. Assist. Corp.*, 902 F.2d at 626 (1990 opinion explaining that under the regulations a reserve fund includes "gifts or grants from other sources" used for Loan Program functions). Second, by the time Congress amended 20 U.S.C. § 1072(g)(1), all but one of the so-called spend-down cases had been decided. In these cases, our sister circuits addressed whether the federal government could require the return of "excess reserve funds," funds accumulated by the guaranty agencies in excess of that needed for Loan Program functions. In each case, it was held that the federal government could require the return of such funds. *See Colorado*, 962 F.2d at 971 (10th Cir.); *Rhode Island Higher Educ. Assistance Auth. v. Sec. U.S. Dept. Educ.*, 929 F.2d 844, 852 (1st Cir. 1991); *Great Lakes*, 911 F.2d at 14-15 (7th Cir.); *Educ. Assist. Corp.*, 902 F.2d at 626-27 (8th Cir.); *Ohio Student Loan Comm'n* ,900 F.2d at 899-900 (6th Cir.); *South Carolina State Educ. Assist. Auth. v. Cavazos*, 897 F.2d 1272, 1276 (4th Cir. 1990).

In several of these cases our sister circuits reached that result by reasoning that reserve fund assets did not constitute private property because of the extensive federal regulation over such assets and the notice provided to the agencies by the breadth of the regulations. *Great Lakes*, 911 F.2d at 14 ("Federal law regulates the reserve fund extensively and it exists because of a federal mandate."); *Educ. Assist. Corp.*, 902 F.2d at 626-27 ("A guaranty agency's 'reserve fund' is entirely a creature of federal regulation . . . . Because of the extensive federal regulation of [the guaranty agency's] reserve

fund, we hold that [the guaranty agency]has no ownership interest in its reserve fund . . . ."); *South Carolina*, 897 F.2d at 1276 ("We agree that the regulations which completely control the reserve funds' uses are the sort of 'existing rules or understandings' which prevent any guaranty agencies from acquiring an ownership interest in its reserve fund . . . ."); *see also Delaware v. Cavazos*, 723 F. Supp. 234, 240 (D. Del. 1989) ("This extensive regulation over the reserve fund precludes Delaware from claiming that the property in the fund is Delaware's private property."). In addition, in some of the spend-down cases, our sister circuits explicitly recognized that under the regulations the reserve fund of a guaranty agency could contain monies from non-federal or private sources; yet that recognition did not alter the holding that reserve fund assets belong to the federal government. *See Colorado*, 962 F.2d at 970 ("Guaranty agency reserve funds may be and frequently are comprised of federal, non-federal and even private funds."); *Ohio Student Loan Comm'n*, 900 F.2d at 897 (explaining that the particular guaranty agency also "takes in money from non-federal sources."); *see also Puerto Rico Higher Educ. Assist. Corp. v. Riley*, 304 U.S. App. D.C. 72, 10 F.3d 847, 850 (D.C. Cir. 1993) (holding that $9 million capital contribution from private parent corporation could be included in reserve fund because "Congress intended all reserve fund assets, regardless of their source, to factor into the Department's calculations of excess cash reserves") (decided Dec. 10, 1993, after adjournment of first session of 103rd Congress, which amended 20 U.S.C. § 1072(g)(1), *see* 1993 U.S.C.C.A.N. 1088).

While ascertaining congressional intent from Congress's failure to act is a difficult proposition, the Secretary has made a persuasive case for his position.

Congress amended 20 U.S.C. § 1072(g)(1) just as the spend-down cases were coming to an end in the various federal appeals courts, and those cases applied the Secretary's broad regulatory definition of "reserve funds" in reaching their results. Further, in 20 U.S.C. § 1072(g)(1) Congress did place limits on when the Secretary could reach all of the reserve funds--e.g., after a best interest determination--which may have been a step taken in recognition that the spend-down cases could be broadly interpreted to allow the Secretary unfettered access to a guaranty agency's reserve funds.

SLFI points to the legislative history for 20 U.S.C. § 1072(g)(1) to argue for an alternative congressional intent. One sentence in the House conference report states, "It is the conferees further intention that all references to guaranty agencies reserves contained in amendments to section[1072] refer only to the 'Federal portion' of such reserves." H. Conf. Rep. No. 103-213, at 456 (1993), reprinted in ,1993 U.S.C.C.A.N. 1088, 1145. There is, however, no definition of "Federal portion" in the legislative history. While it is possible to infer that "Federal portion" means funds arising from federal sources, this would dramatically narrow the scope of the Secretary's regulations, essentially allowing only the recall of federal advances. *See* 34 C.F.R. § 682.410(a)(1). Further, to adopt SLFI's argument with respect to this bit of legislative history would render the first sentence of 20 U.S.C. § 1072(g)(1) largely superfluous, for it would serve little purpose to legislate that reserve funds belong to the United States if "reserve funds" already means only the "Federal portion." This snippet of legislative history may cast ambiguity on the statutory provision; it does not, however, constitute "clear and certain congressional intent."

Rust, 500 U.S. at 190.

SLFI also relies on 20 U.S.C. § 1072(a)(2) to argue that Congress intended to define "reserve funds" for purposes of 20 U.S.C. § 1072(g)(1) to exclude funds arising from private sources. As amended in 1992, 20 U.S.C. § 1072(a)(2) provides:

> Matching Requirement.--No advance shall be made after June 30, 1968, unless matched by an equal amount from non-Federal sources. Such equal amount may include the unencumbered non-Federal portion of a reserve fund. As used in the preceding sentence, the term "unencumbered non-Federal portion" means the amount (determined as of the time immediately preceding the making of the advance) of the reserve fund less the greater of--
>
> (A) the sum of--
>
> (i) advances made under this section prior to July 1, 1968;
>
> (ii) an amount equal to twice the amount of advances made under this section after June 30, 1968, and before the advance for purposes of which the determination is made; and
>
> (iii) the proceeds of earnings on advances made under this section; or

> (B) any amount which is required to be maintained in such fund pursuant to State law or regulation, or by agreement with lenders, as a reserve against the insurance of outstanding loans.

Except as provided in section [1078(c)(10)(E) or (F)], such unencumbered non-Federal portion shall not be subject to recall, repayment, or recovery by the Secretary.

SLFI argues that the last sentence of this provision means that Congress has evinced a clear intent to prohibit the Secretary from including private-source funds in ascertaining SLFI's "reserve funds." Several considerations lead us to reject SLFI's argument. First, 20 U.S.C. § 1072(g)(1) was amended the year following the amendments to 20 U.S.C. § 1072(a)(2), and 20 U.S.C. § 1072(g)(1) provides that it applies *"notwithstanding any other provision of law." See* Cisneros, 508 U.S. at 18.

Second, 20 U.S.C. § 1072(a)(2) does not actually provide a definition of "reserve fund." Rather, it explains that within a reserve fund there may be something called an "unencumbered non-Federal portion." In turn, the amount of the "unencumbered non-Federal portion" is defined only in terms of a specific formula which is applied "as of the time immediately preceding the making of the advance." 20 U.S.C. § 1072(a)(2). It is not clear from the text of the statute whether this "unencumbered non-Federal portion" is always present in the reserve fund, as asserted by SLFI, or whether it is only created upon application of the formula just prior to the receipt of a specific type of advance. Here, it is undisputed that SLFI never received the type of federal

advance identified in this subsection.

Finally, even if 20 U.S.C. § 1072(a)(2) is applicable to SLFI, the reference to 20 U.S.C. § 1078(c)(10)(E) & (F) likely should be to 20 U.S.C. § 1078(c)(9)(E) & (F), because section 4107(a) of P.L. 103-66 (107 Stat. 368) strikes paragraph (9) of section 1078(c) and redesignates paragraph (10) as paragraph (9) of that section. As discussed above, 20 U.S.C. § 1078(c)(9)(E) & (F) are the provisions that the Secretary may utilize to terminate its agreements with a guaranty agency and gain control over a guaranty agency's functions. As so read, 20 U.S.C. § 1072(a)(2) provides that if the Secretary relies on the statutory procedures for termination, even the "unencumbered non-Federal portion" of a reserve fund is subject to recall. By implication, the entire reserve fund may be regarded as the property of the federal government, but the Secretary may require the entire fund, including the "unencumbered non-Federal portion," only under certain conditions. So interpreted, 20 U.S.C. § 1072(a)(2) is remarkably similar to 20 U.S.C. § 1072(g)(1), which explicitly provides that the reserve fund is the property of the United States, but that it may be required in its entirety only if certain specified conditions--e.g., best interest determination--are met.

While SLFI's arguments do serve to cloud congressional intent, they do not illuminate it. The Act simply does not explicitly define "reserve funds," and the Secretary has the express power to fill such gaps through the promulgation of regulations. SLFI has not established that Congress clearly intended to reject the broad regulatory definition in amending 20 U.S.C. § 1072(g)(1); at most, SLFI has shown that there is an ambiguity. However, that

ambiguity is not for us to clarify; rather, we accord deference to the Secretary's regulations as required by Chevron. *See Mead Corp.*, 121 S. Ct. at 2175.

REVERSED AND REMANDED.

APPENDIX C

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF IDAHO

Case No. CIV 94-0413-S-LMB

[Filed February 7, 2000]

STUDENT LOAN FUND OF IDAHO, INC., a non-profit Idaho corporation,
Plaintiff,

v.

RICHARD W. RILEY, in his official capacity as Secretary of the United States Department of Education; and the UNITED STATES DEPARTMENT OF EDUCATION,
Defendants.

AMENDED JUDGMENT

Pursuant to the Court's Memorandum Decision and Order entered on February 7, 2000, the Judgment dated August 20, 1999, entered in the instant matter is hereby modified as follows:

(1) Plaintiff's receipt of $8,502,832 in future guaranty money shall be conditioned upon Plaintiff's compliance with the following:

(a) hold the future guaranty money in a separate reserve account, exercising whatever responsibilities in connection with that money by which a student loan guaranty agency participating in the Federal Family Education Loan Program is bound with regard to the holding of reserve fund assets;

(b) use the future guaranty money to pay legitimate guaranty claims submitted by the holders of loans guaranteed under the Federal Family Education Loan Program; and

(c) return to the Department, its designee, or any successor in interest, all future guaranty money, if any, that it holds, along with any earnings on that money, if any, that it holds, which remain after the loans guaranteed by SLFI under the Federal Family Education Loan Program before July 1, 1994, are no longer outstanding.

(2) The above modifications shall only supplement the August 20, 1999 Judgment. Other than the above-stated modifications, the remainder of the August 20, 1999 Judgment shall remain in full force and effect.

SO ORDERED this 7th day of February, 2000.

/s/_____
LARRY M. BOYLE
UNITED STATES MAGISTRATE JUDGE

APPENDIX D

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF IDAHO

Case No. CIV 94-0413-S-LMB

[Filed February 7, 2000]

STUDENT LOAN FUND OF IDAHO, INC., a non-profit Idaho corporation,
Plaintiff,

v.

RICHARD W. RILEY, in his official capacity as Secretary of the United States Department of Education; and the UNITED STATES DEPARTMENT OF EDUCATION,
Defendants.

MEMORANDUM DECISION AND ORDER

Currently pending before the Court is Defendants' and Counterclaim-Plaintiffs' Motion to Amend Findings of Fact and to Alter or Amend the Judgment (Docket No.321).

Having carefully reviewed the record, considered oral arguments, and otherwise being fully advised, the Court enters the following Memorandum Decision and Order.

I.

BACKGROUND

The factual background of this case is set forth at length in the Court's Findings of Fact, Conclusions of Law, Memorandum Decision and Order dated August 20, 1999 (Docket No. 318) and, therefore, need not be set forth extensively herein. However, the Court will set forth an abbreviated version of the facts, enough to understand the context which gives rise to Defendants'/Counterclaimants' Motion to Amend.

In July 1978, the Student Loan Fund of Idaho, Inc. (SLFI) and the Commissioner of Education (the predecessor to the United States Department of Education which is a defendant herein) entered into five written agreements, patterned after the requirements of the Higher Education Act (HEA), wherein SLFI agreed to conduct a program of loan insurance with eligible lenders which complied with the provisions of the HEA in exchange for receiving an extension of federal credit through governmental reinsurance of its insurance obligations to the lenders. The parties' agreements provided that SLFI would be entitled to reimbursement for all or part of the losses that SLFI incurred as a result of student borrower defaults on insured loans. Under the agreements, SLFI was also entitled to receive federal advances designed to assist in the establishment of funds to hold in reserve for payments to lenders as a result of student loan repayment defaults. The agreements provided that either party had a right to terminate the relationship existing between the parties upon written notice.

On April 22, 1994, SLFI gave the United States Department of Education (Department) written notice of its intent to terminate the parties' agreements and indicated that it would not guarantee any additional loans after June 30, 1994. Thereafter, on September 13, 1994, the Department issued a verbal directive to SLFI to immediately transfer all of SLFI's outstanding loan portfolio and guaranty agency assets to a successor guaranty agency designated by the Department. In response to SLFI's refusal to comply with the Department's directive, the Department took certain action which restricted SLFI from accessing its bank accounts. The Department also initiated an offset against SLFI by ceasing to make reimbursement payments in order to recover what the Department asserted was federal property that was wrongfully being held by SLFI. Finally, the Department suspended and proposed for debarment from federal student loan programs the members of the SLFI board of directors, unilaterally transferred SLFI's guarantees to its successor guaranty agency, and authorized lenders to sell SLFI guaranteed loans to ineligible lenders.

On September 20, 1994, SLFI filed the instant action against Defendants alleging a breach of contract claim. According to SLFI, notwithstanding its termination of the parties' agreements in 1994, the Department remained obligated to service and guarantee loans which pre-dated SLFI's termination. SLFI argued that the Department breached its contractual obligation to reimburse SLFI for the losses on the student loans guaranteed by SLFI prior to July 1, 1994. SLFI also argued that the Department breached it contractual obligations by not following the necessary procedures for instituting an offset against a debt which the Department asserted was owed by SLFI. Furthermore, SLFI

argued that the Department breached its contractual obligations by demanding a transfer of all SLFI funds and assets, claiming that such funds and assets were federal property, without first satisfying the statutory prerequisites set forth in § 422(g) of the HEA for requiring such a transfer. Finally, SLFI argued that the Department breached the parties' agreements when it unilaterally transferred guarantees issued by SLFI to another guaranty agency.

In response, the Department argued that its actions were reasonable and made to ensure that all federal property and reserve fund assets were returned to the government. On February 27, 1995, the Department filed a counterclaim against SLFI asserting that SLFI breached a fiduciary duty owed to the Department (which duty arose from the parties' agreements) by refusing to comply with the Department's order to transfer the funds to a successor guaranty agency. The Department further maintained that, as a fiduciary of the Department, SLFI was required to provide an accounting of all reserve fund assets and transfer all such assets to the Department.

On October 19, 1998, a nine-day court trial was commenced. After the conclusion of the trial, the Court entered its Findings of Fact, Conclusions of Law, Memorandum Decision and Order, ruling in favor of SLFI on its breach of contract claim in all respects, and denying Defendants' counterclaim. (Docket No. 318).

On September 8, 1999, Defendants filed a Motion to Amend the Findings of Fact and to Alter or Amend the Judgment which is the subject of this Memorandum Decision and Order.

II.

ANALYSIS

A. Issue of Timeliness and Request for Rule 11 Sanctions

Defendants move the Court for an order amending the Findings of Fact pursuant to Fed. R. Civ. P. 52(b) and for an order altering or amending the Judgment pursuant to Fed. R. Civ. P. 59(e). Both Rules 52(b) and 59(e) require that a motion to amend made pursuant to these rules be filed no later than ten (10) days following entry of the judgment.

Plaintiff suggests that Defendants' Motion to Amend may not be timely, depending on what date the Court considers to be the entry date of the judgment. While the docket sheet reflects that the judgment was filed on August 20, 1999, it also indicates that the "entry date" of the judgment is August 24, 1999. If the August 24, 1999 date is considered the entry date as contemplated by Rules 52(b) and 59(e), then Defendants' Motion to Amend is timely (in light of Fed. R. Civ. P. 6 which provides that when the filing requirement is less than eleven (11) days, weekends and holidays are not counted). In this case, not counting the weekends and Labor Day, Defendants' Motion to Amend, which was filed on September 8, 1999, is timely if the entry date is August 24, 1999. However, if the entry date is August 20, 1999, Defendants' Motion to Amend is not timely.

The Court concludes that the proper entry date, as contemplated under Rules 52(b) and 59(e), is the entry date reflected on the docket sheet - which in this case is August 24,

1999. Accordingly, the Court concludes that Defendants' Motion to Amend was timely filed.

In its brief in opposition to Defendants' Motion to Amend, Plaintiff argues that Defendants' Motion to Amend is without a basis in fact or law and is really an attempt to toll the period for filing an appeal in the hopes that SLFI will eventually become destitute and fail to meet its obligations to its lenders. Thus, Plaintiff argues that the Court should impose sanctions under Fed. R. Civ. P. 11, which at a minimum should include a reprimand and the non-tolling of the time for taking an appeal.

In the Court's view, there is nothing to suggest that Defendants' Motion to Amend was brought in bad faith and, thus, no basis exists for awarding Rule 11 sanctions against Defendants. Defendants' Motion to Amend was timely filed; thus, Plaintiff's request for Rule 11 sanctions is denied.

A. Standard for Motions to Amend Under Fed. R. Civ. P. 52(b) and 59

The decision whether to grant a motion to alter or amend findings or the judgment pursuant to Fed. R. Civ. P. 52(b) and 59 is committed to the sound discretion of the trial court. *See Springs v. First Nat'l Bank of Cut Bank,* 835 F.2d 1293 (9th Cir. 1988). The purpose of post-judgment motions to amend under Rules 52(b) and 59 is to give the trial court an opportunity to correct manifest errors of law or fact at trial, allow the presentation of newly discovered evidence, or take other action in the interests of justice. *See Fontenot v. Mesa Petroleum Co.,* 791 F.2d 1207, 1219 (5th Cir. 1986). "This is not to say, however, that a motion to amend should be

employed to introduce evidence that was available at trial but was not proffered, to relitigate old issues, to advance new theories, or to secure a rehearing on the merits." *Id.*

C. Analysis

In support of their Motion to Amend, Defendants contend that the Court failed to address two important issues in its Findings of Fact, Conclusions of Law, Memorandum Decision and Order dated August 20, 1999:

> (1) whether SLFI's termination applied only to future loan guarantees, or whether it applied to all federally guaranteed student loans, including those guaranteed prior to the termination date; and
>
> (2) whether SLFI's termination or the Department's finding that a transfer was in the "best interest" of the Federal Family Education Loan Program constituted an adequate predicate for the Department to require the transfer by SLFI of federal reserve fund assets to the successor guaranty agency.

Defendants also contend that the Court's damage award is flawed, is not supported by the evidence in the record, and could result in a windfall to Plaintiff. The Court will address each of Defendants' claims respectively.

(1) <u>The effect of SLFI's termination</u>

The Court clearly sets forth in its Findings of Fact Nos. 6 and 7 as follows:

> 6. Termination of the agreements between SLFI and the Department did not affect obligations and corresponding contractual rights imposed and held by the respective parties that were in place prior to July 1, 1994.
>
> 7. Notwithstanding SLFI's termination of the agreements and cessation of operations as a guaranty agency under the Guaranteed Student Loan Program, SLFI remained under obligations that it incurred while acting as a guaranty agency under the federal student loan program, specifically, the obligations extended to lenders to insure outstanding student loans against default in repayment and the obligations imposed upon SLFI preparatory to receiving federal reimbursement. Termination did not affect the Department's obligation to comply with SLFI's contractual right to reimbursement for insurance claims paid to lenders.

(Docket No. 318, p. 20). Based upon these Findings of Fact and other related Findings of Fact and Conclusions of Law, it is clear from the Court's August 20, 1999 decision that it found that SLFI's termination only applied to future loan guarantees made after the date of termination and did not apply to those loans guaranteed by SLFI prior to the

termination date.

Nevertheless, Defendants contend that the Court's decision is deficient because it does not explain why SLFI is entitled to reinsurance for loans guaranteed before termination, much less reinsurance for future guaranty payments. According to Defendants, the Court should have found that the liability for the old loan guarantees made by SLFI prior to the date of termination was that of the successor guaranty agency, not SLFI's. Defendants also contend that there is substantial evidence in the record that SLFI intended to terminate its agreements with Defendants both prospectively and retroactively.

In opposition to Defendants' Motion to Amend, Plaintiff argues that the Court's Findings of Fact Nos. 1, 2, 3, 4, 5, 6, 7 and 9 and its Conclusions of Law No. 24 provide sufficient support for the Court's express conclusion that SLFI's termination did not affect the parties' obligations in place at the time of termination. Plaintiff argues that Defendants are merely dissatisfied with the Court's findings and conclusions and that this is not a proper basis to grant a motion to amend under either Rule 52(a) or 59(e).

In the Court's view, the August 20, 1999 decision adequately sets forth the basis for finding that SLFI's termination did not affect Defendants' contractual obligation to reimburse SLFI for any insurance claims paid to lenders as a result of the loan guarantees made by SLFI prior to the date of termination. In the introduction of its decision, the Court specifically referred to the termination clause in the parties' agreements which provided, in relevant part, as follows:

> The Commissioner's obligations to make payments, as provided for in this Agreement, shall extend only with respect to loans insured by the Agency prior to termination of this agreement or prior to the expiration of the authority provided in the Act.
>
> ...Termination shall not affect obligations incurred under this Agreement by either party before the effective date of termination.

(Docket No. 318, pp. 56). The Court explained in the "Summary" section of its decision that, in resolving the instant controversy, it relied upon "fundamental notions of basic contract and property law. Obligations and promises were made and extended between the respective parties and, based upon the provisions of their contract, obligations and liabilities were incurred with third parties." (Docket No. 318, p.25).

The Court also explained that its decision had "been guided by statutory and regulatory provisions, together with corresponding Congressional intent relating to the Higher Education Act," *(Id.*, pp. 25-26), and made specific reference to 20 U.S.C. § 1078 (c)(1)(A) in the introduction section of its decision, which provides that a "guaranty agency shall be deemed to have a contractual right against the United States, during the life of such loan, to receive reimbursement according to the provisions of this subsection." (Docket No. 318, p. 6). Relying on fundamental notions of contract law, the specific language in the parties' termination clause, and the statutory provision in 20 U.S.C. § 1078 (c)(1)(A), the Court found that SLFI's termination did not extinguish the Department's contractual obligation (which was in place prior

to termination) to reimburse SLFI for insurance claims paid to lenders as a result of the loan guarantees made by SLFI prior to the date of termination.

The Court's August 20, 1999 decision adequately addresses the effect of SLFI's termination and clearly sets forth the basis for its finding in this regard. Accordingly , Defendants' Motion to Amend with respect to this issue is denied.

(2) Defendants' Counterclaim

In their counterclaim against Plaintiff, Defendants asserted that Plaintiff breached its fiduciary duty by refusing to comply with the Department's administrative order to transfer all of its funds and assets to the successor guaranty agency. Defendants further maintained that, as a fiduciary of the Department, SLFI was required to provide an accounting of all reserve fund assets and transfer all such assets to the Department.

In support of their Motion to Amend, Defendants contend that the Court's August 20, 1999 decision apparently rejects their counterclaim, but does not explain the basis for the Court's rejection. According to Defendants, the only reference the Court makes to Defendants' counterclaim is in the introduction to the Court's Findings of Fact where the Court states:

> At the outset it must be pointed out that to the extent the Court has concluded that the evidence in the record does not support certain claims or counterclaims made by therespective

> parties, they will not be included in the Court's Findings of Fact or otherwise referenced herein. In the event such claims or counter-claims are not contained in these Findings of Fact, it is not an oversight or unintentional omission. Rather, the failure to mention an event or a series of events in these Findings is an indication that the evidence does not support a finding and conclusion in favor of the claim or counter-claim.

(Docket No. 318, p. 19). Defendants argue that this statement is not sufficient for appellate review -- in other words, it does not meet the requirements of Fed. R. Civ. P. 52(a) which requires adequate factual findings that would allow an appellate court to review the basis for the Court's rejection of Defendants' counterclaim.

In response, Plaintiff argues that Defendants' counterclaim seeking a transfer of federal funds and assets to the successor guaranty agency is moot in light of the Court's conclusion that SLFI does not have any federal funds or assets. Plaintiff contends that Defendants are attempting to reargue matters that were raised and proven at trial by SLFI for which Defendants failed to establish any contrary evidence. Specifically, Plaintiff argues that the testimony of several of its witnesses and one of Defendants' own witnesses established that SLFI does not have any federal funds or assets, and that Defendants failed to introduce any evidence to the contrary. In order to succeed on Defendants' counterclaim requesting a transfer, Defendants were required to provide evidence of one of two alternate predicates: (1) that the transfer was ordered in a manner sufficiently connected with

a termination to render it legitimate, or (2) that the Department made a determination that the transfer would be in the "best interest" of the Federal Family Education Loan (FFEL) program. *See* 20 U.S.C.§ 1072 (g)(1). Plaintiff contends that Defendants failed to present any evidence that SLFI terminated its operations and, according to Plaintiff, Defendants admitted at trial that no "best interest" determination was made. Thus, Plaintiff argues that, even assuming Defendants' counterclaim is not moot, the Court's ultimate rejection of the counterclaim is supported by the record.

Defendants, on the other hand, argue that their counterclaim is not moot and, at the very least, the Court should have addressed their request for an accounting. Defendants argue that in the Court's earlier Memorandum Decision and Order dated September 14, 1995, the Court ruled that such assets as insurance premiums, collections on FFEL-guaranteed loans and administrative cost allowances which were held in SLFI's operating fund constituted reserve fund assets which belonged to the government. Defendants refer to SLFI's internal financial statements which identify revenues consisting of insurance premiums, loan recoveries and administrative costs. Defendants recognize the Court's conclusion that the support fees paid by the Student Loan Fund of Idaho Marketing Association, Inc. (IMA) to SLFI were private funds not subject to recovery by the government, but nevertheless claim that the evidence shows that SLFI's reserve fund contains assets that go beyond these support fees from IMA. Thus, Defendants argue that, at a minimum, they are entitled to an accounting as to the assets in SLFI's reserve fund.

In its August 20, 1999 decision, the Court made the following findings of fact:

> 10. SLFI received $250,000 in federal advances pursuant to § 422(c) of the Higher Education Act. These advances constituted reserve fund assets which were credited to SLFI's reserve fund. Inasmuch as the federal advances were federal property and held in SLFI's reserve fund, SLFI did not hold a property interest in the funds. However, the entire balance of § 422(c) advances was repaid to the Department.
>
> 15. On September 30, 1993, SLFI held $2,388,012 in its guaranty agency reserve fund. One year later, on September 30, 1994, SLFI held $2, 108,021 in its reserve fund. After SLFI terminated its agreements with the Department, it continued to fulfill insurance obligations incurred prior to the date of termination. *However, in complying with the obligation to make insurance payments to lenders, SLFI's guaranty agency reserve fund was depleted.* By September 30, 1994, SLFI had used $215,875 in excess of its reserve fund to comply with obligations incurred under the federal student loan program.

(Docket No. 318, pp. 21, 23) (emphasis added). These factual findings are supported by substantial evidence in the record.

Because the evidence indicates that SLFI's guaranty agency reserve fund was totally depleted, it follows that Defendants' request for a court order requiring that SLFI transfer to the government all reserve fund assets is moot. Furthermore, Defendants' request for an accounting is moot as well, since there are no reserve fund assets that can be accounted for. Because Defendants' request for a transfer and an accounting are .moot, there is no need for the Court to address whether Defendants have met their burden in establishing either of the two alternate predicates necessary for requiring a transfer under 20 U.S.C. § 1072 (g)(1). The Court made it clear in the introduction to its Findings of Fact that, where the evidence in the record did not support a claim or counterclaim made by the respective parties, said claim or counterclaim would not be addressed in either the Court's Findings of Fact or "otherwise referenced herein." (Docket No. 318, p. 19).

In sum, the Court's August 20, 1999 decision clearly sets forth certain factual findings, which are supported by substantial evidence in the record, that render Defendants' counterclaim moot. The Court need not make express findings or conclusions with respect to a moot issue. For this reason, Defendants' Motion to Amend the Court's findings with respect to Defendants' counterclaim is denied.

(3) Plaintiff's Damage Award

The Court's damage award with respect to Defendants' failure to reimburse SLFI is based on the Court's factual finding that SLFI was required to use private funds to pay its insurance obligations owed to third-party lenders with respect to the student loans it had guaranteed prior the date of

termination (Findings of Fact No. 19), and that SLFI would be required to use private funds to fulfill future federal guarantees (Findings of Fact No. 20). The Court concluded that, where SLFI had used private, non-federal funds to comply with its insurance obligations as a former guaranty agency, SLFI had a continuing fight to reimbursement of these private funds. (Findings of Fact No. 18).

In support of their Motion to Amend, Defendants argue that SLFI never provided evidence that demonstrated that any of the guaranty claims it paid after the termination were paid with the support fees from IMA (*i.e.*, private funds) as opposed to money which came from collections or from some other source which the Court has held belongs to the government (*i.e.*, insurance premiums or administrative cost allowances). Defendants also argue that SLFI did not establish that future guaranty payments would only be paid with support fees from IMA. Because SLFI has not established how much of its private assets have been or will be used to pay guaranty claims, Defendants argue that the Court's award of damages with respect to the Department's failure to reimburse should be vacated.

In the alternative, Defendants argue that should the Court's award of future damages stand, the Court should, at the very least, modify the Judgment to require that SLFI abide by the program rules applicable to maintaining a federal reserve fund. Specifically, Defendants argue that SLFI's receipt of the future damage award should be conditioned upon SLFI's promise to:

> (1) hold the future guaranty money in a separate reserve account, exercising whatever

> responsibilities in connection with that money by which a student loan guaranty agency participating in the Federal Family Education Loan Program is bound with regard to the holding of reserve fund assets;
>
> (2) use the future guaranty money to pay legitimate guaranty claims submitted by the holders of loans guaranteed under the Federal Family Education Loan Program; and
>
> (3) return to the Department, its designee, or any successor in interest, all future guaranty money, if any, that it holds, along with any earnings on that money, if any, that it holds, which remain after the loans guaranteed by SLFI under the Federal Family Education Loan Program before July 1, 1994, are no longer outstanding;
>
> (4) pay to the Department amounts equal to the equitable share to which the government would be entitled pursuant to 20 U.S.C. § 1078(c) with respect to any collections as to which that equitable share has not been paid.

Defendants argue that these restrictions are necessary for ensuring that SLFI uses its future damage award to actually pay future guaranty claims and does not receive a windfall. Defendants argue that these restrictions are also necessary to protect the government from having to pay for the future guarantees twice. In this respect, Defendants argue that if SLFI does not pay the future guaranty claims, the lenders

could seek payment from the Department pursuant to 20 U.S.C. § 1082(o), in which case the Department would have to pay the guarantees twice (once to SLFI and again to the lenders).

In response, Plaintiff argues that the restrictions proposed by Defendants are not warranted by the evidence (*i.e.*, there is no evidence that suggests that Plaintiff will not pay the future guaranty claims), nor are the restrictions necessary in light of the fact that Plaintiff is already contractually obligated to make the future guaranty claims to eligible third-party lenders. Furthermore, with respect to Defendants' initial argument that Plaintiff failed to demonstrate how much of its private assets have been or will be used to pay guaranty claims, Plaintiff argues that matters such as collections, insurance premiums, etc. were all a part of its damage calculations at trial and Defendants never challenged these particular items; therefore, Defendants are stopped from now arguing that these particular items were not properly considered below.

A review of the trial transcript and the record as a whole indicates that, although Defendants challenged Plaintiff's damage calculations on several grounds, they never specifically raised the argument that Plaintiff's damage claim was flawed on the basis that Plaintiff had failed to demonstrate how much of its private assets (*i.e.*, the support fees from IMA) have been used to pay guaranty claims or will be used to pay future guaranty claims. Because Defendants did not raise this particular argument at trial, they are precluded from asserting it now in support of their Motion to Amend. *See Fontenot*, 791 F.2d at 1219 (holding that a motion to amend should not be employed to "introduce evidence that was

available at trial but was not proffered" or "to relitigate old issues").

A review of the record also reveals that Defendants never raised the argument that Plaintiff's receipt of future damages should be conditioned upon Plaintiff's agreement to comply with certain program rules applicable to maintaining a federal reserve fund. Nevertheless, the Court is of the view that, in the interests of justice, some conditions should be imposed upon Plaintiff's receipt of future damages which would ensure against Plaintiff receiving a windfall. The Court recognizes that Plaintiff could receive a windfall if for example future default rates fall below the historical default rates which Plaintiff's expert employed in calculating Plaintiff's future damages. Should future default rates fall below the historical default rates, Plaintiff would have guaranty money left over (after the loans it guaranteed under the FFEL program before July 1, 1994 are no longer outstanding) which rightfully belongs to the government. To ensure that this does not happen, the Court concludes that certain conditions should be imposed upon Plaintiff's receipt of its future damage award.

In the Court's view, the first three conditions proposed by Defendants are reasonable conditions which would ensure against a windfall to Plaintiff. Thus, the Court orders that, in addition to the August 20, 1999 judgment entered in favor of Plaintiff, Plaintiff's receipt of $8,502,832 in future guaranty money shall be conditioned upon Plaintiff's compliance with the following:

> (1) hold the future guaranty money in a separate reserve account, exercising whatever

> responsibilities in connection with that money by which a student loan guaranty agency participating in the Federal Family Education Loan Program is bound with regard to the holding of reserve fund assets;
>
> (2) use the future guaranty money to pay legitimate guaranty claims submitted by the holders of loans guaranteed under the Federal Family Education Loan Program; and
>
> (3) return to the Department, its designee, or any successor in interest, all future guaranty money, if any, that it holds, along with any earnings on that money, if any, that it holds, which remain after the loans guaranteed by SLFI under the Federal Family Education Loan Program before July 1, 1994 are no longer outstanding.

However, with respect to Defendants' fourth proposed condition, the Court will deny Defendants' request that it order Plaintiff to pay to the Department an amount equal to the equitable shares contemplated under 20 U.S.C. § 1078(c). In the Court's view, this request or condition does not specifically relate to the issue of a windfall to Plaintiff, but rather deals with an offset to the amount of future damages calculated by Plaintiff. Defendants could have raised this argument of an offset to Plaintiff's alleged amount of future damages at trial, but they did not.[1] Accordingly, they should

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[1] In fact, Plaintiff argues that its expert considered the issue of equitable shares when calculating Plaintiff's future damages

not be able to raise the argument for the first time in support of their Motion to Amend. *See Fontenot,* 791 F.2d at 1219.

III.

ORDER

Based on the foregoing, IT IS HEREBY ORDERED that Defendants' and Counterclaim-Plaintiffs' Motion to Amend Findings of Fact and to Alter or Amend the Judgment (Docket No. 321) is GRANTED in part and DENIED in part. The Motion is granted to the limited extent that the Court orders that, in addition to the August 20, 1999 judgment entered in favor of Plaintiff which shall remain in full force and effect, Plaintiff's receipt of $8,502,832 in future guaranty money shall be conditioned upon Plaintiff' s compliance with the following:

> (1) hold the future guaranty money in a separate reserve account, exercising whatever responsibilities in connection with that money by which a student loan guaranty agency participating in the Federal Family Education Loan Program is bound with regard to the holding of reserve fund assets;
>
> (2) use the future guaranty money to pay legitimate guaranty claims submitted by the holders of loans guaranteed under the Federal

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at trial; yet Defendant never challenged this element of Plaintiff's damage calculation.

Family Education Loan Program; and

(3) return to the Department, its designee, or any successor in interest, all future guaranty money, if any, that it holds, along with any earnings on that money, if any, that it holds, which remain after the loans guaranteed by SLFI under the Federal Family Education Loan Program before July 1, 1994, are no longer outstanding.

The remainder of Defendants' Motion to Amend is denied.

SO ORDERED this 7th day of February, 2000.

/s/_____
LARRY M. BOYLE
UNITED STATES MAGISTRATE JUDGE

APPENDIX E

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF IDAHO

Case No. CIV 94-0413-S-LMB

[Filed August 23, 1999]

STUDENT LOAN FUND OF IDAHO, INC., a non-profit Idaho corporation, Plaintiff,	)
v.	)
RICHARD W. RILEY, in his official capacity as Secretary of the United States Department of Education; and the UNITED STATES DEPARTMENT OF EDUCATION, Defendants.	)

FINDINGS OF FACT, CONCLUSIONS OF LAW, MEMORANDUM DECISION AND ORDER

I.

INTRODUCTION

The Higher Education Act was enacted in 1965, 20 U.S.C. §§ 1070, *et seq.*, in order to create a guaranteed student loan program designed to provide financial assistance

to students pursuing post-secondary education. Section 421 of the Act allows the Secretary of the United States Department of Education "to encourage States and nonprofit private institutions and organizations establish adequate loan insurance programs for students in eligible institutions." 20 U.S.C. § 1071(a)(1)(A).

The Student Loan Fund of Idaho, Inc., (SLFI) a nonprofit institution, was incorporated in 1978 for the purpose of promoting education for Idaho students. On June 13, 1978, SLFI was designated by the Governor of Idaho as Idaho's guaranty agency. To that end, in July 1978, SLFI and the Commissioner of Education (the predecessor to the Secretary of Education) entered into five written agreements, patterned after the requirements of the Higher Education Act (HEA), which were intended to govern the relationship between SLFI, as a Federal Family Education Loan Program Guaranty Agency (FFEL), and the Department of Education (Department).

SLFI agreed to conduct a program of loan insurance with lenders which complied with the provisions of the agreements and the HEA while receiving an extension of federal credit through governmental reinsurance of SLFI's insurance obligations to lenders. Further, the agreements provided that SLFI would be entitled to reimbursement for all or part of the losses that SLFI incurred as a result of student borrower defaults on insured loans. In addition to the agreement to receive federal reimbursement payments, SLF1 was also entitled to, and did receive, federal advances designed to assist in the establishment of funds to hold in reserve for payments to lenders as a result of student loan

repayment defaults. By entering into the agreements, SLFI made assurances that it would comply with the statutory requirements imposed by the HEA as well as corresponding regulations as they existed at the time of the agreements or as they were otherwise amended. Finally, the agreements provided that either party had a right to terminate the relationship existing between the Department and SLFI upon written notice.

SLF1 was also required to deposit or credit all federal payments or revenues received from the Department in a reserve fund. To comply with that requirement, SLFI created and maintained a separation of the revenue received which fell within the definition, as understood by SLFI, of reserve fund assets and revenue from other sources which was collected in SLFI's operating fund.

In 1979, the Student Loan Fund of Idaho Marketing Association, Inc. (IMA) was established in order to create a secondary market for lenders participating in the guaranteed student loan program. Although SLFI and IMA are two separate corporations, their relationship is extremely close and does raise concerns regarding potential conflicts of interest inasmuch as the corporations share corporate officers and employees. In this regard, IMA paid SLFI the salaries and benefits of the SLFI employees performing tasks for IMA, as well as a loan servicing fee based upon a percentage of the outstanding loan portfolio of IMA, made to assure the continued viability of SLFI as a corporation.

Under the loan insurance program implemented between SLFI and third-party lenders, the lenders made loans

to eligible students, or their parents, in order to finance higher education expenses. Under the insurance program, lenders would pay SLFI an insurance premium while, in turn, SLFI agreed to purchase student loans that defaulted during the loan repayment period. Pursuant to SLFI's agreement with the Department, to the extent that SLFI was required to purchase a loan in default from a third-party lender, SLFI obtained federal reimbursement for the amount of insurance proceeds used.

As a result of changes to the HEA due to the Omnibus Budget Reconciliation Act of 1993, SLFI determined that it would be unable to continue operations as a guaranty agency and continue to meet obligations with lenders on previously insured loans. In early April 1994, SLFI and the Northwest Education Loan Association (NELA) reached a tentative agreement that SLFI would transfer to NELA all outstanding SLFI guarantees and all reserve funds and that NELA would allow SLFI, or an assignee of SLFI, to service the outstanding guaranteed loans assumed by NELA. Thereafter, on April 22, 1994, SLFI provided written notice to the Department of its intention to terminate their agreements and indicated that it would not guarantee any additional loans after June 30, 1994.

SLFI maintains that it intended to terminate the agreement only to the extent that it would no longer guarantee new loans, but would continue to guarantee all outstanding loans in existence prior to June 30, 1994. According to the Department, SLFI terminated the entire agreement and, as a result, ceased to operate as a guaranty agency in the FFEL program. On April 26, 1994, SLF1 and NELA informed the Department that they had agreed that the outstanding portfolio

of loans guaranteed by SLFI would be transferred to NELA along with related reserve funds. On April 28, 1994, in response to the April 26 letter from SLFI and NELA, the Department asserted that the purported agreement violated the provisions of the HEA and terminated the agreement directing both SLFI and NELA not to take any additional steps to finalize the proposed agreement under threat of criminal prosecution.

On May 31, 1994, after reviewing NELA as a successor guaranty agency, the Department designated NELA as the guaranty agency for the State of Idaho and directed SLFI to transfer all outstanding guarantees, the defaulted loan portfolio and all reserve funds and applicable assets to NELA. On July 1, 1994, SLFI ceased issuing loan guarantees for any new loans, and has not issued loan guarantees for any new loans since that date. However, with the exception of $81,841.00, SLFI has not transferred any reserve fund assets to the Department or its designee since June 30, 1994.

On September 13, 1994, the Department issued a verbal directive to SLFI requiring the immediate transfer of all assets, including all existing funds as well as all real and personal property, to NELA. In a letter dated September 20, 1994, Larry Oxendine, Acting Director, Guarantor and Lender Oversight Staff, directed SLF1 to transfer all of its assets to NELA including defaulted loans, outstanding loan guarantees, all funds regardless of form as well as all physical assets wholly or partially owned by SLFI and further directed SLFI to refrain from using, transferring or otherwise creating an expenditure for any funds held by SLFI.

On November 3, 1994, Oxendine again directed SLFI to transfer all of the outstanding loan portfolio and guaranty agency assets to NELA and, in light of SLFI's refusal to comply, directed SLFI to remove SLFI's Corporate Director, Carrol Lee Lawhorn, from any involvement relating to the expenditure, use or transfer of SLFI's funds or assets. Also during November of 1994, Robert Armstrong, on behalf of the Department, contacted financial institutions with SLFI accounts and provided a copy of a letter written by Oxendine indicating that all of SLFI's assets held in such accounts were federal property and should be transferred to NELA. Although the financial institutions did not transfer the accounts as requested, Armstrong was successful in having the institutions restrict SLFI's access to the assets held in the accounts.

In addition to placing restrictions upon the use of SLFI's accounts, the Department initiated an offset against SLFI by ceasing to make reimbursement payments in order to recover what the Department asserted was federal property that was wrongfully being held by SLFI. Further, the Department suspended and proposed for debarment from federal student loan programs the members of the SLFI board of directors, unilaterally transferred SLFI's guarantees to NELA, and authorized lenders to sell SLFI guaranteed loans to ineligible lenders.

On September 20, 1994, SLFI filed the instant action against the Department and the Secretary of the United States Department of Education, Richard W. Riley. SLFI alleges that Defendants' actions exceeded statutory and contractual authority under the HEA and the agreements between the parties. SLF1 maintains that the agreements satisfy all of the

elements necessary for contract formation. SLFI asserts that notwithstanding the termination of the agreement with the Department which became effective July 1, 1994, it remains obligated to service and guarantee loans which pre-date termination. The termination clause contained in the agreement expressly states:

> The Commissioner's obligations to make payments, as provided for in this Agreement, shall extend only with respect to loans insured by the Agency prior to termination of this agreement or prior to the expiration of the authority provided in the Act.
>
> This Agreement may be terminated by either party upon not less than 60 days written notice to the other party, except that the Commissioner may terminate this Agreement only for cause. Termination shall not affect obligations incurred under this Agreement by either party before the effective date of termination.

According to SLF1, notwithstanding SLFI's notice of intent to decline to guarantee any additional loans after June 30, 1994, it had the contractual right to continue to guarantee student loans existing prior to the date of termination and the Department breached its obligation to reimburse SLFI for losses on student loans guaranteed by SLFI prior to July 1, 1994. Further, the HEA provides that a "guaranty agency shall be deemed to have a contractual right against the United States, during the life of such loan, to receive reimbursement

according to the provisions of this subsection." 20 U.S.C. § 1078 (c)(1)(A). As a result, SLFI maintains that the Department is required to make reimbursement payments for losses on all loans insured by SLFI prior to July 1, 1994.

SLFI further asserts that the Department breached its contractual obligations by violating federal law when it instituted an offset against a debt it asserted was owed by SLFI. Because the procedures required to institute an offset were not followed, SLFI claims that the Department breached the agreement causing damage. In addition, SLFI maintains that the Department breached its contractual duties by demanding the transfer of all SLFI funds and assets and claiming that such funds and assets were federal property without first satisfying the statutory prerequisites set forth in § 422(g) of the HEA for requiring such a transfer. SLFI also asserts that the portion of the HEA relied upon by the Department does not provide authorization to demand and require SLFI to transfer reserve funds.

SLFI further asserts that the Department breached the agreement when it unilaterally transferred guarantees issued by SLFI to another guaranty agency. SLFI points out that the Department was not a party to the contracts created between SLFI and the lending institutions. After the Department demanded the transfer of all SLFI guarantees to NELA and it became apparent that SLFI would not comply, the Department notified lenders that their guarantees had been transferred to NELA. Further, SLFI alleges that the Department authorized NELA to pay lender claims and submit claims for reinsurance for loans actually insured by SLFI. As a result of Defendants' conduct, SLFI maintains that it has been significantly impaired

in its ability to perform its obligations and has consequently been unable to reap the benefits resulting from the fulfillment of its contractual duties.

The Department denies that it acted outside the scope of its statutory authority or otherwise failed to comply with obligations in place at the time of SLFI's termination of operation as a guaranty agency. According to the Department, the actions that it has undertaken have been reasonable and made to ensure that all federal property and reserve fund assets are returned to the government. The Department claims that SLFI has wrongfully asserted ownership over federal property and has violated provisions of the HEA and the agreements entered into between the respective parties. On February 27, 1995, the Department filed a counter-claim against SLFI asserting that SLFI had entered into contractual relations with the Department which required SLFI to abide by all applicable statutory and regulatory requirements relating to SLFI's participation in the student loan program. According to the Department, all money obtained by SLFI from any source in connection with the student loan program constituted federal reserve fund assets and SLFI's failure to comply with an administrative order and transfer the funds after its participation as a guaranty agency had terminated constituted a breach of the fiduciary duties owed to the Department. The Department further maintains that, as a fiduciary of the Department, SLFI should be required to provide an accounting of all reserve fund assets and transfer all such assets to the Department.

SLFI asserts that the demand to transfer all federal property to the Department is moot because it currently does

not hold federal property. SLFI points to § 422(a)(2) of the HEA to establish Congress' express intent that only the federal portion of a guaranty agency's reserve fund, and not the non-federal portion, is subject to recall and that Congress intended that portions of a guaranty agency's reserve fund would maintain a non-federal character. Further, SLFI asserts that all of the federal portion of the reserve funds received has been repaid to the Department.

Defendants maintain that the Court has already held that SLFI does not have a valid property interest in either the reserve funds or to reinsurance payments. Further, Defendants assert that the Court has previously determined that the reserve funds encompass all assets SLFI refuses to transfer and that SLFI is limited to assert only a breach of contract claim for obligations in place at the time of the termination of the agreement between SLFI and the Department.

Defendants take the position that SLFI is required to return all of its reserve funds. Defendants also contend that SLFI does not have a contractual right to continued reinsurance payments, and therefore, may not pursue a breach of contract claim against the Department for instituting the offset, which it maintains was determined by this Court to have been properly conducted. Further, Defendants maintain that SLFI is unable to establish a viable theory of damages and points out that remote and consequential damages are unrecoverable in a common law breach of contract action, especially one against the United States. Finally, Defendants argue that SLFI is unable to establish that the contract damages it seeks were foreseeable at the time the contractual relationship was formed. Inasmuch as SLFI is unable to

provide support for the amount of damages claimed, Defendants assert that SLFI is not entitled to relief.

On October 19, 1998, a nine-day court trial was commenced. After the conclusion of the trial, and after all evidence had been received by the Court, the parties filed post-trial memoranda, including proposed findings of fact and conclusions of law. On April 29, 1999, counsel for the respective parties presented closing argument, after which the Court took the matter under advisement. Accordingly, the matter has been fully submitted and is ready for disposition. After reviewing the evidence presented to the Court, applicable law and the arguments of counsel, the Court enters the following legal authorities, Findings of Fact, Conclusions of Law, Memorandum Decision and Order.

II.

LEGAL AUTHORITY

A. Jurisdiction and Sovereign Immunity

It is established beyond reasonable dispute that a plaintiff may sue the United States only if two conditions are met. First, Congress must have waived sovereign immunity for the lawsuit, and second, Congress must have provided for jurisdiction there. *North Star Alaska v. United States,* 9 F.3d 1430, 1432 (9th Cir. 1993). Accordingly, in order for SLFI to bring the instant breach of contract action in this Court, not only must the Court have jurisdiction over the claims, but the United States must have waived sovereign immunity with respect to those claims.

The district courts have original jurisdiction of all civil actions arising under the Constitution, laws, or treaties of the United States. 28 U.S.C. § 1331. Specifically applicable to this action, § 432 of the HEA provides that the Secretary of Education "may ... be sued ... in any district court of the United States," and that "such district courts shall have jurisdiction of civil actions arising under this part without regard to the amount in controversy." 20 U.S.C. § 1082(a)(2).

B. Contract Law

When the United States enters into contract relations, its rights and duties therein are governed generally by the law applicable to contracts between private individuals. *See Perry v. United States,* 294 U.S. 330, 352, 55 S.Ct. 432, 435, 79 L.Ed. 912 (1935) ("When the United States, with constitutional authority, makes contracts, it has rights and incurs responsibilities similar to those of individuals who are parties to such instruments. There is no difference ... except that the United States cannot be sued without its consent."). "Congress is not free to entice a party into a contract by making certain pledges and then withdraw those pledges." *Education Assistance Corp. v. Cavazos,* 902 F.2d 617, 629-30 (8th Cir. 1990) (citing *Perry,* 294 U.S. at 350, 55 S.Ct. at 434). Thus, after entering into a contract, the government may not alter its contractual obligations without "remain[ing] liable for breach of contract where its legislation is directed at repudiating its prior contractual agreements." *Winstar Corp. v. United States,* 64 F.3d 1531, 1551 (Fed. Cir. 1995).

Fundamental contract law provides:

> [A] contract is a legally enforceable agreement between two or more parties. The essential elements necessary to transform an agreement into a legally enforceable contract include, among other things, competent parties, a subject matter, legal consideration, mutuality of agreement, and mutuality of obligation. The element of mutuality of agreement, or mutual assent, frequently has been referred to in the law as a "meeting of the minds" of the parties to the contract or agreement. To create a contract, then, the minds of the parties must meet as to every essential term of the proposed contract, and there must be a clear and unequivocal acceptance of a certain and definite offer in order that a mere agreement may become a contract. Therefore, it is necessary, among other things, that the minds of the parties meet as to the essential terms of the proposed contract. There must be a reciprocal assent to a certain and definite proposition between them. As long as any substantial or material matters are left open for further negotiations or consideration on an essential and necessary element of a proposed contract, the contract is not complete, and the agreement, if there has been such, is not enforceable as a legally enforceable contract.

Joseph v. Donover Co., 261 F.2d 812, 824 n. 11 (9th Cir. 1958).

The interpretation of contractual agreements between the United States and private parties is governed by federal law because such contracts are "entered into pursuant to authority conferred by federal statute and, ultimately, by the Constitution." *United States v. Seckinger,* 397 U.S. 203, 209-10, 90 S.Ct. 880, 884, 25 L.Ed.2d 224 (1970). In applying federal law to determine the meaning of contractual terms, federal courts are "guided by the general principles that have evolved concerning the interpretation of contractual provisions." *Id.* at 210, 90 S.Ct. at 884.

Among these principles is the proposition that when an ambiguity exists in a contract, federal courts are to apply "the general maxim that a contract should be construed most strongly against the drafter, which in [Seckinger] was the United States." *Id.* "Whether an ambiguity exists is a question of law." *Saavedra v. Donovan,* 700 F.2d 496, 500 (9th Cir. 1983) (citing *United States v. Sacramento Mun. Util. Dist.,* 652 F.2d 1341, 1343-44 (9th Cir. 1981)). "A contract is ambiguous if reasonable people could find its terms susceptible to more than one interpretation." *Kennewick Irrigation Dist. v. United States,* 880 F.2d 1018, 1032 (9th Cir. 1989) (citing *Castaneda v. Dura-Vent Corp.,* 648 F.2d 612, 619 (9th Cir. 1981)). '"The fact that the parties dispute a contract's meaning does not establish that the contract is ambiguous,"' *id.* (quoting *International Union of Bricklayers & Allied Craftsman Local No. 2 v. Martin Jaska, Inc.,* 752 F.2d 1401, 1406 (9th Cir. 1985)), but "'[a] written contract must be read as a whole and every part interpreted with

reference to the whole ... [with p]reference ... given to reasonable interpretations as opposed to those that are unreasonable, or that would make the contract illusory."' *Id.* (quoting *Shakey's Inc. v. Cobalt,* 704 F.2d 426, 434 (9th Cir. 1983)). The United States Court of Appeals for the Ninth Circuit has provided that governmental contracts should be interpreted against the backdrop of the legislative scheme that authorized them. *Peterson v. United States Dep't of the Interior,* 899 F.2d 799, 807 (9th Cir. 1990).

A. Damages

"The general rule in common law breach of contract cases is to award damages that will place the injured party in as good a position as he or she would have been had the breaching party fully performed." *Estate of Berg v. United States,* 687 F.2d 377, 379 (Ct. Cl. 1982) (citing *Northern Helex Co. v. United States,* 524 F.2d 707, 713 (Ct. Cl. 1975), *cert. denied,* 429 U.S. 866, 97 S.Ct. 176 (1976)). "Furthermore, remote and consequential damages are not recoverable in a common-law suit for breach of contract." *Northern Helex,* 524 F.2d at 719 (citing *Globe Ref Co. v. Landa Cotton Oil Co.,* 190 U.S. 540, 543, 23 S.Ct. 754, 47 L.Ed. 1171 (1903)). "This is especially true in suits against the United States for the recovery of common-law damages" *Id.* (citing Ramsey v. United States, 101 F.Supp. 353 (1951), *cert. denied,* 343 U.S. 977, 72 S.Ct. 1072, 96 L.Ed. 1369 (1952)); *see also Wells Fargo Bank N.A. v. United States,* 88 F.3d 1012, 1021 (Fed. Cir. 1996), *cert. denied,* 520 U.S. 1116, 117 S.Ct. 1245 (1997). Finally, in order to establish damages resulting from a breach of contract, a party must establish that such damages were foreseeable at the time of the

contract's creation. *Globe Ref* Co., 190 U.S. at 544, 23 S.Ct. at 755-56.

D. The HEA and the Contract Terms Between SLFI and the Department

In this instant action, the agreements entered into between the respective parties, as well as applicable portions of the HEA, describe the relationship between a guaranty agency and the Department of Education under the student loan program. Based upon the provisions of the loan program, eligible third-party lenders would extend loans to qualifying students. These lenders would receive a guarantee by guaranty agencies which, when a student defaulted in repaying a student loan, would insure the third-party lender against loss. To comply with its insurance obligations owed to third-party lenders, a guaranty agency would make loan insurance payments from the assets included within its reserve fund. Once a claim was paid by the guaranty agency, the Department of Education would then reimburse the guaranty agency for the funds taken out of the agency's reserve fund.

The regulatory definition of the assets that fall within a guaranty agency's reserve fund are those which include:

> The total amount of insurance premiums collected; ... [f]unds received from a State for the agency's guaranty activities, including matching funds under section 422(a) of the Act; ... [f]ederal advances obtained under sections 422(a) and (c) of the Act; ... [f]ederal payments for default, bankruptcy, death,

> disability, closed schools, and false certification claims; ... [s]upplemental preclaims assistance payments; ... [a]dministrative cost allowance payments received under § 682.407 and transitional support payments received under section 458(a) of the Act; ... [i]nvestment earnings on the reserve fund; and ... [o]ther funds received by the guaranty agency from any source for the agency's guaranty activities.

34 C.F.R. § 682.410(a)(l)(i)-(ix).

> In 1987, the HEA was amended in order to limit the amount of cash reserves a ... guaranty agency may maintain in its reserve fund. [The 1987 amendments] were adopted after the Comptroller General reported to Congress that guaranty agencies had built up unnecessarily large cash reserves and some were using the funds for non-GSL purposes .... The amendments require[d] the Secretary to determine a maximum cash reserve for each agency ... and to recover the amount of reserves in excess of that maximum amount.

Education Assistance Corp. v. Cavazos, 902 F.2d 617, 620 (8th Cir. 1990). Guaranty agencies challenged the amendments on two bases, first they argued that they had property interests in the cash reserves contained within an agency's reserve fund; second, they asserted that the statute allowing the Secretary to determine an excess amount and

demand transfer of the excess cash reserves to the Department violated Fifth Amendment protections prohibiting the deprivation of property without due process of law. The Fifth Amendment challenges to the amendments have been labeled the "spend-down" cases.

On September 14, 1995, this Court issued a Memorandum Decision and Order in which it concluded that SLFI, as a guaranty agency, did not have sufficient property rights to the assets contained in its reserve fund to implicate the protections of the Fifth Amendment. Memorandum Decision and Order, pp. 17-21 (Docket No. 100). *See also* Memorandum Decision and Order, p. 10, ¶ ii - p. 16 (Docket No. 235). The Court's decision was based upon (1) the reasoning of the spend-down cases *(i.e.* that the nature of the guaranteed student loan program militates against a determination that reserve fund assets are private property), (2) the extensive federal regulation of guaranty agency reserve funds and (3) the assertion that, although reserve funds are comprised of assets from many sources, the source of reserve fund assets is substantially from the federal government. The issues raised in this instant action, however, were not before the courts in resolving the spend-down cases, specifically, (1) whether private funds from a private source received by a guarantee agency fall within a guaranty agency's reserve fund, (2) whether the regulations defining reserve fund assets implemented by the Department were reasonable and based upon the provisions of the HEA, (3) whether a guaranty agency has sufficient property interests in non-federal reserve fund assets used to comply with insurance obligations to implicate Fifth Amendment protections, and ultimately, (4) whether it has a right to seek reimbursement for the

expenditure of private funds to comply with federal loan guarantees. Thus, the spend-down cases are not instructive with respect to the issues in the present action.

Section 422 of the HEA relates to federal advances that may be made to a guaranty agency's reserve fund. 20 U.S.C. § 1072. Federal advances made under § 422(a) require an equal advance to be made from non-federal sources. 20 U.S.C. § 1072(a)(2). The non-federal advances may be made from any non-federal source including the "unencumbered non-Federal portion of a reserve fund." 20 U.S.C. § 1072(a)(2). Further, Congress has declared that "[e]xcept as provided in section 1078 (c)(9)(E) or (F) of this title, such unencumbered non-Federal portion shall not be subject to recall, repayment, or recovery by the Secretary." 20 U.S.C. § 1072(a)(2) (Supp. 1994).

A guaranty agency's reserve fund includes, by statutory definition, assets "received by the guaranty agency from any source for the agency's guaranty activities." 34 C.F.R. § 682.410(a)(1)(ix). Congress has indicated that a guaranty agency may use an unencumbered non-federal portion of its reserve fund as a non-federal source of funds. By implication, Congress has indicated that non-federal assets may be credited to an agency's reserve and retain their essential character as private assets and remain free from federal reserve fund encumbrances. *See* 20 U.S.C. § 1072(a)(2). However, Congress has not expressly indicated what assets may be credited to the reserve fund of a guaranty agency and retain an unencumbered non-federal character. Yet, based upon the scope of the regulatory definition, and the position asserted by the Department in this instant action, any

non-federal assets credited to a guaranty agency's reserve fund would be deemed a reserve fund asset, subject to extensive regulation, thus leaving SLFI without sufficient interests to the assets to implicate property rights deserving of Fifth Amendment protections.

In addition to the requirement that SLF1 maintain a reserve fund, the agreements and corresponding statutory provisions provided that SLFI would have a right to seek reimbursement from the government for payments made on its insurance obligations to lenders to cover student loan defaults. Congress expressly provided that a "guaranty agency shall be deemed to have a contractual right against the United States, during the life of such loan, to receive reimbursement ... Upon receipt of an accurate and complete request by a guaranty agency for reimbursement with respect to such losses, the Secretary shall pay promptly and without administrative delay." 20 U.S.C. § 1078(c)(1)(A) (Supp. 1994). The agreement entered into between the respective parties to this instant action relating to federal reimbursement provides that the agreement could be terminated by either party, that such termination would not affect obligations existing at the time of termination, and that the Department's obligation to make reimbursement payments would extend only to loans insured by SLFI prior to the termination of the agreement.

The agreements between the parties also provide that if the Department terminated the agreements, the termination would not become effective until SLFI was provided reasonable notice and an opportunity for a hearing. Further, § 428 of the HEA allows the Secretary of Education to terminate the agreement between the Department and a

guaranty agency. 20 U.S.C. § 1078. Such action is based upon a determination by the Secretary that the guaranty agency has failed to comply with obligations imposed by the agreement, or is in danger of financial failure, or the action is otherwise necessary to promote the loan program and protect federal interests. 20 U.S.C. § 1078(c)(9)(E)(i)-(vi) (Supp. 1994). If a guaranty agency's agreement is terminated by the Secretary, the Secretary becomes authorized to

> permit the transfer of guarantees to another guaranty agency; ... revoke the reinsurance agreement of the guaranty agency at a specified date, so as to require the merger, consolidation, or termination of the guaranty agency; ... transfer guarantees to the Department of Education for the purpose of payment of such claims and process such claims using the claims standards of the guaranty agency ... [and] use all funds and assets of the guaranty agency to assist in the activities undertaken in accordance with this subparagraph and take appropriate action to require the return, to the guaranty agency or the Secretary, of any funds or assets provided by the guaranty agency, under contract or otherwise, to any person or organization ....

20 U.S.C. § 1078(c)(9)(F)(i)-(vi)(Supp. 1994).

In addition to the ability to terminate the agreement with a guaranty agency, the Secretary may also require a guaranty agency to transfer all of its reserve funds to the

Department. Section 422(g) of the HEA provides that "the Secretary may not require the return of all reserve funds of a guaranty agency to the Secretary unless the Secretary determines that such return is in the best interest of the operation of the program." 20 U.S.C. § 1072(g)(1) (Supp. 1994). A "guaranty agency," for purposes of the HEA, is defined as "any State or nonprofit private institution or organization with which the Secretary has an agreement under section 1078(b) of this title." 20 U.S.C. § 1085(j).

E. Deference to Agency's Statutory Interpretation

In interpreting the statutory and regulatory provisions of the HEA, the Court is required to give deference to the Department's interpretation. The United States Supreme Court has declared:

> When a court reviews an agency's construction of the statute which it administers, it is confronted with two questions. First, always, is the question whether Congress has directly spoken to the precise question at issue. If the intent of Congress is clear, that is the end of the matter; for the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress. If, however, the court determines Congress has not directly addressed the precise question at issue, the court does not simply impose its own construction on the statute, as would be necessary in the absence of an administrative

> interpretation. Rather, if the statute is silent or ambiguous with respect to the specific issue, the question before the court is whether the agency's answer is based on a permissible construction of the statute.

Chevron, U.S.A., Inc. v. Natural Resources Defense Council, 467 U.S. 837, 842-43, 104 S.Ct. 2778, 2780-81, 81 L.Ed.2d 694 (1984).

The deference to be given to an agency's interpretation of the statutory scheme that it has been directed to carry out is based upon the principle that "[t]he power of an administrative agency to administer a congressionally created ... program necessarily requires the formulation of policy and the making of rules to fill any gap left, implicitly or explicitly, by Congress." 467 U.S. at 843, 104 S.Ct. at 2843 (quoting *Morton v. Ruiz,* 415 U.S. 199, 231, 94 S.Ct. 1055, 1072, 39 L.Ed.2d 270 (1974)). When Congress leaves gaps in a program, "there is an express delegation of authority to the agency to elucidate a specific provision of the statute by regulation" and, as such, an agency's regulations promulgated to fill the statutory gap left open by Congress "are given controlling weight unless they are arbitrary, capricious, or manifestly contrary to the statute." *Id.* at 843-44, 104 S.Ct. at 2782. In giving such deference to an agency's interpretation of a congressionally created program, "a court may not substitute its own construction of a statutory provision for a reasonable interpretation made by the administrator of an agency." *Id.* at 844, 104 S.Ct. at 2782.

When confronted with a regulatory interpretation designed to fill a gap in a statutorily created program, a trial court is required to review the interpretation, with the appropriate amount of deference, to the facts of the particular dispute at issue. *United Slates v. Haggar Apparel* Co., _ U.S. _, 119 S.Ct. 1392, 1399, 143 L.Ed.2d 480 (1999). As a result, the appropriate amount of "[d]eference can be given to the regulations without impairing the authority of the court to make factual determinations, and to apply those determinations to the law, de novo." *Id.* Accordingly, "[i]n the process of considering a regulation in relation to specific factual situations, a court may conclude the regulation is inconsistent with the statutory language or is an unreasonable implementation of it. In those instances, the regulation will not control." *Id.*

III.

FINDINGS OF FACT

Having carefully considered the testimony of all the witnesses called at trial, having thoroughly reviewed all of the exhibits admitted into evidence, and having considered controlling legal authority and arguments of counsel, the Court makes the following Findings of Fact and Conclusions of Law pursuant to Federal Rule of Civil Procedure 52(a).

At the outset it must be pointed out that to the extent the Court has concluded that the evidence in the record does not support certain claims or counter-claims made by the respective parties, they will not be included in the Court's Findings of Fact or otherwise referenced herein. In the event

such claims or counter-claims are not contained in these Findings of Fact, it is not an oversight or unintentional omission. Rather, the failure to mention an event or series of events in these Findings is an indication that the evidence does not support a finding and conclusion in favor of the claim or counter-claim The Court's Findings of Fact are as follows:

1. The Higher Education Act provided the Department of Education the constitutional authority to enter into agreements with guaranty agencies for the purposes of inducing such guaranty agencies to participate in the Guaranteed Student Loan Program. Upon entering into the agreements, the respective parties intended to be bound by the obligations referred to in the agreements and valuable consideration was exchanged in relation to the respective promises and obligations given and received pursuant to the agreements.

2. The agreements contemplate that SLFI would engage in a program of loan insurance by entering into contractual relations and incurring obligations with financial institutions who would actually extend loans to eligible students. SLFI also incurred the obligation of insuring the student loans issued by such lenders with extensions of federal credit and purchasing loans from such lenders when the loans were in default of repayment. SLFI received the contractual right to seek from the Department reimbursement of the funds used to purchase loans in default from lenders throughout the lifetime of the loans guaranteed by SLFI.

3. Pursuant to the agreements, the Department incurred the obligation of reimbursing SLFI for insurance

claims that SLFI paid to lenders. SLFI, as a guaranty agency operating under the federal student loan program, was required to credit federal reimbursement payments to its reserve fund.

4. Prior to July 1, 1994, SLFI incurred obligations to lenders to insure loans issued to eligible students under the Guaranteed Student Loan Program. Consequently, prior to July 1, 1994, the Department incurred the obligation to reimburse SLFI for payments made to lenders in fulfillment of SLFI's insurance obligations.

5. On July 1, 1994, with sufficient written notice, SLFI terminated its agreement with the Department. Inasmuch as a guaranty agency is statutorily defined as a private organization "with which the Secretary has an agreement" under the HEA, SLFI ceased operating as a guaranty agency and became a former guaranty agency, or private loan guarantor with existing obligations incurred under the Guaranteed Student Loan Program.

6. Termination of the agreements between SLFI and the Department did not affect obligations and corresponding contractual rights imposed and held by the respective parties that were in place prior to July 1, 1994.

7. Notwithstanding SLFI's termination of the agreements and cessation of operations as a guaranty agency under the Guaranteed Student Loan Program, SLFI remained under obligations that it incurred while acting as a guaranty agency under the federal student loan program, specifically, the obligations extended to lenders to insure outstanding

student loans against default in repayment and the obligations imposed upon SLFI preparatory to receiving federal reimbursement. Termination did not affect the Department's obligation to comply with SLFI's contractual right to reimbursement for insurance claims paid to lenders.

8. A guaranty agency operating under agreements with the Department pursuant to the provisions of the Higher Education Act does not have an enforceable property right to reserve fund assets. Accordingly, a guaranty agency that pays insurance claims to lenders out of federal reserve fund assets does not have an enforceable contractual right to require the Department to reimburse the guaranty agency with federal assets.

9. Similarly, a former guaranty agency, or private loan guarantor, does no have enforceable property interests in federal reserve fund assets. As a result, a former guaranty agency which complies with insurance obligations extended to lenders while acting as a guaranty agency by paying insurance claims on defaulted loans with federal reserve fund assets does not have an enforceable contractual right to federal reimbursement of the federal reserve funds paid to lenders. However, a former guaranty agency, or private loan guarantor, which complies with obligations to insure federally guaranteed student loans by using private funds or assets to pay insurance claims filed by lenders holding student loans in default does have an enforceable contractual right to seek federal reimbursement from the Department for private funds or assets used to perform an obligation incurred under the Higher Education Act.

10. SLFI received $250,000 in federal advances pursuant to § 422(c) of the Higher Education Act. These advances constituted reserve fund assets which were credited to SLFI's reserve fund. Inasmuch as the federal advances were federal property and held in SLFI's reserve fund, SLFI did not hold a property interest in the funds. However, the entire balance of § 422(c) advances was repaid to the Department.

11. The Student Loan Fund of Idaho Marketing Association (IMA) was established with private funds and the assets acquired and generated through IMA's activities in the secondary market are non-federal assets. IMA paid support fees to SLF1 while SLF1 was acting as a guaranty for the purpose of assuring the continued financial viability of SLFI as a guaranty agency. Further, in 1985, IMA made a payment to SLFI in the amount of $500,000 in order to strengthen SLFI's guaranty agency reserve fund. The support fees and $500,000 payment from IMA to SLFI fall within the regulatory definition of reserve fund assets subject to federal regulation and property interests.

12. Congress has not indicated whether payments of private funds from a private entity to a guaranty agency fall within the definition of a reserve fund asset and are encumbered by federal property interests pursuant to the Higher Education Act.

13. Notwithstanding the Department's assertion that all funds received by SLFI while acting as a guaranty agency relating to its operations as a guaranty agency, regardless of their origin, are federal reserve fund assets, the Court finds that, after reviewing the Department's interpretation of the

HEA and applicable regulations, the Department's position is inconsistent with Congressional intent and the underlying purposes of the HEA. The Court finds that, based upon the facts of this instant action, private funds paid from a private entity to a guaranty agency, even though related to the guaranty agency's operations under the Guaranteed Student Loan Program, fall within the definition of what Congress has indicated is the unencumbered non-federal portion of a guaranty agency's reserve fund. In this regard, the Court finds and thus has concluded that the payment of private funds by a private entity to a non-federal guaranty agency does not change the fundamental character of the funds from private to federal property even though the funds may be received by the private guaranty agency for purposes relating to its involvement in a federal student loan program. Accordingly, the Court finds that the support fees paid by IMA and received by SLFI, including the $500,000 payment to SLF1 in 1985, are private assets and are not subject to recall, repayment, or recovery by the Secretary.

14. During its years of operation as a guaranty agency participating in the Guaranteed Student Loan Program, SLFI received substantial non-program related funds from private sources. The Court finds that the Department's application of the regulations and assertion that these assets fall within the scope of a guaranty agency's reserve fund is unreasonable as applied to the facts involved in this instant action. Accordingly, the Court finds that these assets consist of unencumbered non-federal assets held by a guaranty agency.

15. On September 30, 1993, SLFI held $2,388,012 in its guaranty agency reserve fund. One year later, on

September 30, 1994, SLFI held $2,108,021 in its reserve fund. After SLFI terminated its agreements with the Department, it continued to fulfill insurance obligations incurred prior to the date of termination. However, in complying with the obligation to make insurance payments to lenders, SLFI's guaranty agency reserve fund was depleted. By September 30, 1994, SLFI had used $215,875 in excess of its reserve fund to comply with obligations incurred under the federal student loan program.

16. The Department reimbursed SLFI for insurance claims paid to lenders until October 1994. Thereafter, in November 1994, the Department instituted an offset by withholding reimbursement payments in an attempt to recover federal reserve fund assets the Department maintained were held by SLFI. Notwithstanding the institution of the offset, the Department did pay reimbursement claims made by SLFI in January and February of 1995. However, no other reimbursement payments have been made by the Department.

17. To the extent that federal reserve funds were used by SLFI after the date of termination to fulfill insurance obligations incurred in relation to a federal student loan program, SLFI, acting as a former guaranty agency or private loan insurer, does not have a right to reimbursement of those federal funds.

18. In order to comply with the continuing insurance obligations owed to third-party lenders, SLF1 was required to pay lender insurance claims in compliance with the federal loan guaranty out of private funds. Inasmuch as private non-federal funds were used to comply with SLFI's insurance

obligations, the Court finds that SLFI, as a former guaranty agency, has a continuing right to reimbursement for the amount of private funds used to fulfill SLFI's insurance obligations relating to federal loan guarantees.

19. As of March 1998, SLFI has used $7,652,671 of private funds to comply with its insurance obligations owed to lenders under the federal student loan program; SLFI has not received reimbursement for these funds from the Department of Education.

20. SLFI has a continuing right to be reimbursed for the expenditure of private funds to fulfill federal guarantees extended to third-party lenders pursuant to the insurance obligations SLFI entered into based upon the agreements with the Department of Education and the Higher Education Act. The Court finds that the present value of projected use of private funds to fulfill federal loan guarantees in the future is $8,502,832.

21. Inasmuch as the Court has found that SLFI's termination of the agreements with the Department has not impaired its contractual rights relating to loan insurance contracts entered into with third-party lenders, the Court finds that the Department's unilateral transfer of the guarantees issued by SLFI to third-party lenders violated SLFI's contractual rights and caused SLFI damage in the amount of $345,000.

IV.

CONCLUSIONS OF LAW

After reviewing the evidentiary record, considering the positions asserted by counsel for the respective parties, applicable law and fundamental legal principles, the Court enters the following conclusions of law:

22. To the extent any findings of fact are deemed to be conclusions of law, they are incorporated by reference into these conclusions of law.

23. This Court has jurisdiction to hear the instant action pursuant to 28 U.S.C. 1331 and Fed. R.Civ. P. 73(b), and Congress has waived sovereign immunity to be sued pursuant to 20 U.S.C. § 1082(a)(2). However, the waiver of sovereign immunity allowing for suits to be filed against the Secretary of Education under the Higher Education Act does not allow the institution of an injunction against the Secretary.

24. SLFI and the Department of Education entered into enforceable contracts. The Department of Education's refusal to reimburse SLFI for the expenditure of private funds used to fulfill SLFI's obligations owed to third-party lenders, which were incurred prior to July 1, 1994, resulted in a breach of the contractual duties which were unaffected by SLFI's termination of the contractual relationship.

25. The Department of Education's breach of contract for refusing to reimburse SLFI for the expenditure of private funds used to comply with federal loan guarantees has caused,

and will cause, damages to SLFI in the amount of $16,155,503.

26. The Department's unilateral transfer of outstanding loan guarantees insured by SLFI constituted a breach of contract causing damages to SLFI in the amount of $345,000.

SUMMARY

In resolving the instant controversy between a private corporation and an agency of the federal government who entered into contractual relations in order to comply with the policies and requirements of the Higher Education Act, the Court has repeatedly been reminded of fundamental notions of basic contract and property law. Obligations and promises were made and extended between the respective parties and, based upon the provisions of their contract, obligations and liabilities were incurred with third parties. Fundamental considerations of property law have also shaped the Court's determination of the proper scope of SLFI's reserve fund assets based upon the facts as presented in the instant dispute. The Court's review has also been guided by statutory and regulatory provisions, together with corresponding Congressional intent relating to the Higher Education Act.

The issues presented in this matter have been challenging, and considerable deliberation, review, research and analysis have been expended in reaching this final disposition.

Justice Holmes, speaking for the United States Supreme Court in *Rock Island, A. & L.R. Co. v. United*

States, 254 U.S. 141, 153, 41 S.Ct. 55, 56, 65 L.Ed. 188 (1920), stated: "Men must mm square comers when they deal with the Government." In commenting on this statement, Justice Jackson indicated that "[i]t is very well to say that those who deal with the Government should mm square comers. But there is no reason why the square comers should constitute a one-way street." *Federal Crop Ins. Corp. v. Merrill,* 332 U.S. 380, 387-88, 68 S.Ct. 1, 4-5, 92 L.Ed. 10 (1947) (Jackson, J., dissenting).

In this regard, the Court concludes that when an agency of the federal government enters into contractual relations pursuant to a delegation of Congressional authority and provisions of the United States Constitution, it must comply with the obligations it has undertaken. If allowed to enter into a relationship with a private entity with the ability to enforce the terms of the agreement against that party while remaining free to ignore or breach applicable provisions of the agreement, the Court is of the opinion that the government would be allowed to embark upon a one-way street. By requiring the Department of Education to comply with all obligations owed to SLFI, the Court is ensuring that SLFI's contract with the Department is not one-sided, but rather is based upon the requirements of the Higher Education Act and the body of federal law flowing from that legislation.

VI.

ORDER

Based on the foregoing, IT IS HEREBY ORDERED:

1. Plaintiff's claim for damages relating to Defendants' breach of contract is GRANTED. Plaintiff shall be awarded $7,652,671 based upon the Department's failure to reimburse SLFI for private funds used to comply with federal loan guarantees incurred under the Guaranteed Student Loan Program. Further, Plaintiff shall also be awarded damages in the amount of $8,502,832 for projected damages as a result of the Department's refusal to reimburse SLFI for the anticipated use of private funds to comply with federal loan guarantees. Finally, Plaintiff shall be awarded $345,000 in damages as a result of the Department's unilateral transfer of guarantees issued by SLFI to third-party lenders.

2. Defendant Secretary of Education's counter-claim against SLFI is DENIED.

3. To the extent Plaintiff has implicitly sought injunctive relief, it is denied as contemplated by the Anti-Injunction Act, and the relief sought for future damages is granted in the preceding paragraph.

SO ORDERED this 20th day of August, 1999.

/s/_____
LARRY M. BOYLE
UNITED STATES MAGISTRATE JUDGE

APPENDIX F

IN THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF IDAHO

Case No. CV 94-0413-S-LMB

[Filed August 23, 1999]

STUDENT LOAN FUND OF IDAHO, INC., a non-profit Idaho corporation,
Plaintiff,

v.

RICHARD W. RILEY, in his official capacity as Secretary of the United States Department of Education; and the UNITED STATES DEPARTMENT OF EDUCATION,
Defendants.

JUDGMENT

In accordance with the Findings of Fact. Conclusions of Law, Memorandum Decision and Order filed with this Judgment.

IT IS HEREBY ORDERED, ADJUDGED and DECREED that Plaintiff's claim for damages relating to Defendants' breach of contract is GRANTED. Plaintiff shall be awarded $7,652,671 based upon the Department's failure

to reimburse SLFI for private funds used to comply with federal loan guarantees incurred under the Guaranteed Student Loan Program. Further, Plaintiff shall also be awarded damages in the amount of $8,502,832 for projected damages as a result of the Department's refusal to reimburse SLFI for the anticipated use of private funds to comply with federal loan guarantees.

IT IS FURTHER ORDERED that Plaintiff shall be awarded $345,000 in damages as a result of the Department's unilateral transfer of guarantees issued by SLFI to third-party lenders.

SO ORDERED this 20th day of August, 1999

/s/_____
LARRY M. BOYLE
United States Magistrate Judge

APPENDIX G

IN THE UNITED STATES COURT OF APPEALS

No. 95-36179
D.C. No. CV- 94-00413-LMB

[Filed December 13, 1996]

STUDENT LOAN FUND OF IDAHO, INC., a non-profit Idaho corporation,
Plaintiff,

v.

RICHARD W. RILEY, in his official capacity as Secretary of the United States Department of Education; and the UNITED STATES DEPARTMENT OF EDUCATION,
Defendants.

MEMORANDUM*

* This disposition is not appropriate for publication and may not be cited to or by the courts of this circuit except as provided by Ninth Circuit Rule 36-3.

Court of Appeals Memorandum - 12/13/96

Appeal from the United States District Court
for the District of Idaho
Larry M. Boyle, Magistrate Judge, Presiding

Argued and Submitted September 17, 1996
Seattle, Washington

Before: WRIGHT, SCHROEDER and KLEINFELD, Circuit Judges.

Appellant SLFI correctly argues that partial summary judgment was erroneous because the statutory condition was not satisfied. The Higher Education Act prohibits the Secretary from requiring the return of all guaranty agency reserve funds "unless the Secretary determines that such return is in the best interest of the operation of the program . . . or to ensure the proper maintenance of such agency's funds or assets or the orderly termination of the guaranty agency's operations and the liquidation of its assets." 20 U.S.C. S 1072(g)(1). Appellee argues that SLFI terminated its operations and that the Secretary made a "best interest" determination.

There was at least a genuine issue of fact as to whether SLFI had terminated its operations. SLFI evidently sought to continue performing certain responsibilities regarding existing loans, but to guarantee no future loans. The agency officials apparently did not wish to allow this arrangement. Appellee failed to establish that there was a termination.

There was no evidence that the Secretary had made a "best interest" determination. Appellee's argument relies on there having been such a determination. Appellee argues that

"1072(g) provides DoE with complete authority to terminate SLFI's participation entirely and to seek transfer of all reserve funds and outstanding loan portfolio if such action 'is in the best interest of the operation of the [FFELP] * * *.'" Appellee argues that the May 16 and September 20 letters from the Department to SLFI "demonstrate that DoE had determined that a guarantee agency that was completely in the program ... rather than an agency that was half in and half out, as SLFI claims it was proposing, was in the best interest of the program."

The May 16 letter construes an SLFI letter as notice of termination, and demands access to various books and records in order to "determine the contractual obligations that will be transferred." The September 20 letter, signed by the Acting Director, Guarantor and Lending Oversight Staff, expresses disagreement with SLFI's position that certain assets are not government property, and purports to order SLFI to transfer all assets.

These letters do not satisfy the statutory condition that "the Secretary determines that such return is in the best interest of the operation of the program." While appellee is correct in saying that the statute requires no particular form, it does require that the Secretary make the "best interest" determination. The letters do not purport to make such a determination. They assume the determination has been made and direct SLFI to take actions required of an agency after that determination. They do not establish that the Secretary made such a determination. Our attention has not been directed to any other evidence that the Secretary made the determination required by 20 U.S.C. § 1072(g) (1). It was appellee's burden to prove that this statutory "best interest"

determination had been made, and it offered no evidence to prove it, so summary judgment could not properly be granted in favor of appellee.

Because the evidence did not establish that the statutory condition had been met, the partial summary judgment must be reversed and the permanent injunction vacated. We do not reach the difficult question of which assets SLFI could be required to return or transfer had there been such a determination: all assets listed in 34 C.F.R. 682.410(a)(1), only assets defined in 20 U.S.C. S 1072(a) as "non-federal," or some other denotation. We intimate no view on this question.

We do not reach the question raised by SLFI, of whether the district court erred in denying its motion to amend its complaint. We lack jurisdiction to review that denial because SLFI's entire action has not been dismissed, and none of the relevant exceptions to the general rule that such claims must be appealed after final judgment are applicable. *See Telluride Management Solutions. Inc. v. Telluride Investment Group,* 55 F.3d 463, 466 (9th Cir. 1995). We also do not decide whether the district court erred in denying SLFI's motion for partial summary judgment and writ of mandamus. A denial of a motion for summary judgment is an interlocutory order that cannot be appealed before entry of a final judgment. *Hopkins v. City of Sierra Vista,* 931 F.2d 524, 529 (9th Cir. 1991). Now that the "best interest" determination issue is resolved, the matters raised in this motion will be before the district court for its consideration in light of our decision.

The grant of summary judgment in favor of the Secretary is REVERSED, and the injunction based on it is VACATED.

APPENDIX H

STATUTORY AND REGULATORY PROVISIONS

20 U.S.C. §1071(a)

(a) PURPOSE; DISCRIMINATION PROHIBITED. -

(1) Purpose. - The purpose of this part is to enable the Secretary -

(A) to encourage States and nonprofit private institutions and organizations to establish adequate loan insurance programs for students in eligible institutions (as defined in section 435),

(B) to provide a Federal program of student loan insurance for students or lenders who do not have reasonable access to a State or private nonprofit program of student loan insurance covered by an agreement under section 428(b),

(C) to pay a portion of the interest on loans to qualified students which are insured under this part, and

(D) to guarantee a portion of each loan insured under a program of a State or of a nonprofit private institution or organization which meets the requirements of section 428(a)(1)(B).

20 U.S.C. §1072(a)(2)

(2) Matching Requirement. -No advance shall be made after June 30, 1968, unless matched by an equal amount from non-Federal sources. Such equal amount may include the unencumbered non-Federal portion of a reserve fund. As used in the preceding sentence, the term "unencumbered non-Federal portion" means the amount (determined as of the time immediately preceding the making of the advance) of the reserve fund less the greater of-

(A) the sum of-

(i) advances made under this section prior to July 1, 1968;

(ii) an amount equal to twice the amount of advances made under this section after June 30, 1968, and before the advance for purposes of which the determination is made; and

(iii) the proceeds of earnings on advances made under this section;

or

(B) any amount which is required to be maintained in such fund pursuant to State law or regulation, or by agreement with lenders, as a reserve against the insurance of outstanding loans.

Except as provided in section 428(c)(9)(E) or (F), such unencumbered non-Federal portion shall not oe subject to

recall, repayment, or recovery by the Secretary.

20 U.S.C. §1072(e)(2) & (5) - self repealing effective Sept. 30, 1989

(2) Recovery Of Excess Cash Reserves. - The Secretary shall not later than March 31, 1988, determine for each guaranty agency the maximum cash reserve permitted under paragraph (1) for fiscal year 1986. Subject to paragraph (3) and (4), if the Secretary determines that any guaranty agency had, at the end of fiscal year 1986, a cash reserve that exceeded such maximum, the Secretary shall direct the agency to eliminate such excess by any one or more of the following methods, as selected by the guaranty agency:

(A) by repaying any advances to such agency made by the Secretary under this section that are not required to be repaid under subsection (d);

(B) by withholding and canceling claims for reimbursement otherwise payable under section 428(c)(1);

(C) by reducing the amount of payments for which application will be made by such agency under section 428(f); or

(D) by any other method or reducing payments from or increasing payments to the Federal Government, including payment of additional reinsurance fees in addition to the fees required by section 428(c)(9), as proposed by the agency and agreed to by the Secretary.

***

(5) Definitions. - As used in this subsection -

(A) the 'cash reserves' for any guaranty agency for any fiscal year are equal to the agency's cumulative cash receipts less the agency's cumulative cash disbursements at the end of such fiscal year;

(B) the 'total reserves' for any guaranty agency for any fiscal year are equal to the agency's cash reserves plus the agency's cumulative accounts receivable less the agency's accounts payable, as of the end of such fiscal year;

(C) the term 'cumulative cash receipts' includes such receipts as insurance premiums, Federal reinsurance payments, and collections on defaulted loans;

(D) the term 'cumulative cash disbursements' includes such disbursements as payments for default claims, repayment of Federal advances, transfers to other State activities, and payment of collection costs and other operating costs.

(E) the term 'accounts receivable' includes Federal reinsurance payments and administrative cost allowances owed but not yet paid to the guaranty agency, as of the end of a fiscal year; and

(F) the term 'accounts payable' includes collections and reinsurance fees due (but not paid) to the Department of Education, as of the end of a fiscal year.

20 U.S.C. §1072(g)(1)

(1) Authority To Recover Funds. - Notwithstanding any other provision of law, the reserve funds of the guaranty agencies, and any assets purchased with such reserve funds, regardless of who holds or controls the reserves or assets, shall be considered to be the property of the United States to be used in the operation of the program authorized by this part or the program authorized by part D of this title. However, the Secretary may not require the return of all reserve funds of a guaranty agency to the Secretary unless the Secretary determines that such return is in the best interest of the operation of the program authorized by this part or the program authorized by part D of this title, or to ensure the proper maintenance of such agency's funds or assets or the orderly termination of the guaranty agency's operations and the liquidation of its assets. The reserves shall be maintained by each guaranty agency to pay program expenses and contingent liabilities, as authorized by the Secretary, except that -

(A) the Secretary may direct a guaranty agency to return to the Secretary a portion of its reserve fund which the Secretary determines is unnecessary to pay the program expenses and contingent liabilities of the guaranty agency;

(B) the Secretary may direct the guaranty agency to require the return, to the guaranty agency or to the Secretary, of any reserve funds or assets held by, or under the control of, any other entity, which the Secretary determines are necessary to pay the program expenses and contingent liabilities of the guaranty agency, or which are required for the orderly termination of the guaranty agency's operations and

liquidation of its assets;

(C) the Secretary may direct a guaranty agency, or such agency's officers or directors, to cease any activities involving expenditure, use or transfer of the guaranty agency's reserve funds or assets which the Secretary determines is a misapplication, misuse, or improper expenditure of such funds or assets; and

(D) any such determination under subparagraph (A) or (B) shall be based on standards prescribed by regulations that are developed through negotiated rulemaking and that include procedures for administrative due process.

20 U.S.C. §1078(c)(1)(A) - in part

(1) Authority To Enter Into Agreements. - (A) The Secretary may enter into a guaranty agreement with any guaranty agency, whereby the Secretary shall undertake to reimburse it, under such terms and conditions as the Secretary may establish, with respect to losses (resulting from the default of the student borrower) on the unpaid balance of the principal and accrued interest of any insured loan. The guaranty agency shall, be deemed to have a contractual right against the United States, during the life of such loan, to receive reimbursement according to the provisions of this subsection. Upon receipt of an accurate and complete request by a guaranty agency for reimbursement with respect to such losses, the Secretary shall pay promptly and without administrative delay ....

20 U.S.C. § 1078(c)(8)(A)

(8) Assignment To Protect Federal Fiscal Interest. - (A) If the Secretary determines that the protection of the Federal fiscal interest so requires, a guaranty agency shall assign to the Secretary any loan of which it is the holder and for which the Secretary has made a payment pursuant to paragraph (1) of this subsection.

20 U.S.C. § 1078(c)(9)(E)

(E) The Secretary may terminate a guaranty agency's agreement in accordance with subparagraph (F) if-

(i) a guaranty agency required to submit a management plan under this paragraph fails to submit a plan that is acceptable to the Secretary;

(ii) the Secretary determines that a guaranty agency has failed to improve substantially its administrative and financial condition;

(iii) the Secretary determines that the guaranty agency is in danger of financial collapse;

(iv) the Secretary determines that such action is necessary to protect the Federal fiscal interest;

(v) the Secretary determines that such action is necessary to ensure the continued availability of loans to student or parent borrowers; or

(vi) the Secretary determines that such action is necessary to ensure an orderly transition from the loan programs under this part to the direct student loan programs under part D of this title.

20 U.S.C. § 1078(c)(9)(F)

(F) If a guaranty agency's agreement under this subsection is terminated pursuant to subparagraph (E), then the Secretary shall assume responsibility for all functions of the guaranty agency under the loan insurance program of such agency. In performing such functions the Secretary is authorized to -

(i) permit the transfer of guarantees to another guaranty agency;

(ii) revoke the reinsurance agreement of the guarantees agency at a specified date, so as to require the merger, consolidation, or termination of the guaranty agency;

(iii) transfer guarantees to the Department or Education for purpose of payment of such claims and process such claims using the claims standards of the guaranty agency, if such standards are determined by the Secretary to be in compliance with this Act;

(iv) design and implement a plan to restore the guaranty agency's viability;

(v) provide the guaranty agency with additional advance funds in accordance with section 422(c)(7), with such restrictions on the use of such funds as is determined

appropriate by the Secretary, in order to -

(I) meet the immediate cash needs of the guaranty agency;

(II) ensure the uninterrupted payment of claims; or

(III) ensure that the guaranty agency will make loans as the lender-of-last-resort, in accordance with subsection (j);

(vi) use all funds and assets of the guaranty agency to assist in the activities undertaken in accordance with this subparagraph and take appropriate action to require the return, to the guaranty agency or the Secretary, of any funds or assets provided by the guaranty agency, under contract or otherwise, to any person or organization; or

(vii) take any other action the Secretary determines necessary to ensure the continued availability of loans made under this part to residents of the State or States in which the guaranty agency did business, the full honoring of all guarantees issued by the guaranty agency prior to the Secretary's assumption of the functions of such guaranty agency, and the proper servicing of loans guaranteed by the guaranty agency prior to the Secretary's assumption of the functions of such agency, to avoid disruption of the loan program, and to ensure an orderly transition from the loan programs under this part to the direct student loan programs under part D of this title.

20 U.S.C. §1082(o)

(o) Consequences of Guaranty Agency Insolvency. - In the event that the Secretary has determined that a guaranty agency is unable to meet its insurance obligations under this part, the holder of loans insured by the guaranty agency may submit insurance claims directly to the Secretary and the Secretary shall pay to the holder the full insurance obligation of the guaranty agency, in accordance with insurance requirements no more stringent than those of the guaranty agency. Such arrangements shall continue until the Secretary is satisfied that the insurance obligations have been transferred to another guarantor who can meet those obligations or a successor will assume the outstanding insurance obligations.

34 C.F.R. 682.410(a) (1992)

(a) Fiscal requirements - (1) Reserve fund assets. The guaranty agency shall establish and maintain a reserve fund to be used solely for the FFEL program to which the guaranty agency shall credit -

(i) Federal advances obtained and matching funds required under section 422(a) of the Act;

(ii) Funds appropriated by a State for the agency's loan guarantee program;

(iii) Federal advances obtained under section 422(c) of the Act;

(iv) Funds received by the guaranty agency as loan insurance premiums;

(v) Administrative cost allowances received by the guaranty agency under § 682.407;

(vi) Funds received by the guaranty agency for the agency's loan guaranty program from gift, grant, or other sources;

(vii) Funds collected on FFEL loans;

(viii) Death, disability, bankruptcy, and reinsurance payments received from the Secretary; and

(ix) Investment earnings on the reserve fund.

(2) Uses of reserve fund assets. Except as provided in paragraph (a)(3)-(a)(5) of this section, a guaranty agency may use the assets of the reserve fund established under paragraph (a)(1) of this section only to-

(i) Pay default claims;

(ii) Pay death, disability, and bankruptcy claims;

(iii) Refund overpayments of insurance premiums;

(iv) Pay to the Secretary the Secretary's equitable share of borrower payments;

(v) Repay advances and other funds owed to the Secretary; and

(vi) Make payments to lenders that participate in the loan referral service under section 428(e) of the Act.

APPENDIX I

LEGISLATIVE HISTORY

**S. Rep. No. 94-882, 94th Cong. 2nd Sess.
vol. 4, p. 20-25 (1976), reprinted in 1976
U.S.C.C.A.N. p. 4732-4737 (Emphasis added)**

...[p. 4732] On March 15, 1976, Senator Nunn and Senator Percy on behalf of the Government Operations Committee wrote to Senator Pell, Chairman of the Education Subcommittee, reporting on the results of their oversight hearings. A complete text of their letter follows:

[p. 4733] United States Senate
Committee on Government Operations
Senate Permanent Subcommittee on Investigations
(Pursuant to Sec. 4.9 Res. 49 94th Congress.)
Washington, D.C. 205510

March 15, 1976

The Honorable Claiborne Pell
Chairman, Subcommittee on Education
Committee on Labor & Public Welfare
United states Senate
Washington, D. C. 20510

Dear Senator Pell:

As you know, the Senate Permanent Subcommittee on Investigations has held a series of hearings into fraud and

abuse in the administration of the Federally Guaranteed Student Loan Program. During these hearings, we had the very helpful counsel of Senator Javits, who so ably serves with you on the Education Subcommittee. During our discussions, Senator Javits suggested that we offer your Subcommittee our thoughts on possible legislative initiatives that would appear warranted to correct many of the abuses uncovered during our hearings.

Knowing of your own dedication to this very important program and with deep respect for the leadership role you have played on the Education Subcommittee, we submit for your consideration the legislative proposals outlined below. We will certainly make Subcommittee staff available to meet with your staff to expand upon these proposals and discuss other relevant material which has come to our attention in the course of our investigation.

LIMITING POTENTIAL FOR FUTURE LOSSES

As testimony made clear during the hearings of the Investigations Subcommittee, **default rates are running much higher in the direct, federally-insured part of the GSL program than they are in the state-run program. Under the state program the federal government acts as a reinsurer rather than as a direct insurer**. Although the initial concept of the program was to help middle-income students, [p. 4734] the emphasis has shifted so that a large number of beneficiaries are lower income persons. It was originally anticipated that outright grant programs, with no anticipated repayment, were for the use of these most-disadvantaged students.

At the same time, the original goal of trying to encourage state programs has apparently been abandoned in favor of the direct federally-insured lending program. As a result, only 25 states now operate their own guaranteed student loan program.

To remedy these problems, Congress could pass legislation establishing a date after which the Department of Health, Education and Welfare would no longer directly insure loans. Instead, emphasis would be shifted to state programs. **Accordingly, legislation should also be contemplated to encourage the other 25 states to set up their own programs.**

A principal reason that many states do not operate their own student loan program is the HEW collection policy. In the state-run programs, the federal government reimburses the state 80 per cent of a defaulted loan. This leaves the state with a 20 per cent exposure. However, under existing procedures, if the state collects any money it must turn it over to the federal government until the entire federal obligation is liquidated. Such a policy is a disincentive for state action. **If this policy were modified to provide an equitable sharing of collections between the state and the federal government, more states could be expected to inaugurate their own programs and strengthen existing programs.**

Legislation must also be considered to authorize a study of how to encourage more state-run programs. For example, the federally-guaranteed portion could be increased and/or the federal government could reimburse the state for a percentage of its collection costs.

Your Subcommittee might also consider providing a bonus to states which run their own insured-loan program under the State Incentive Grant Program in which all 50 states now participate.

An alternative would be to limit the total liability of the state and federal governments in the direct loan system to 80 or 90 per cent of the loan, making the lender responsible for 10 or 20 per cent of the liability. But, realistically speaking, this would undoubtedly result in a severe curtailment of the program unless accompanied by some companion inducement to banks to continue to write these loans.

[p. 4735] Finally, consideration should be given to eliminating proprietary and correspondence schools as lenders under the program. In most state programs such schools are not permitted to be lenders, although a student could obtain a loan from another source to enable him to take courses at such schools as lenders is one reason for the better performance of state-run programs. On the other hand, we have heard the counter-argument that such schools offer constructive courses which would not be available to students unless such institutions were permitted to continue as lenders. In any event, it would seem that such institutions should be permitted to serve as lenders only after the most careful scrutiny.

ENFORCEMENT AND COMPLIANCE

It was clear from testimony that the Office of Education has been less than efficient in its administration of the program and woefully lacking in professional personnel who will dutifully enforce existing laws and regulations. It is, therefore, suggested that a most important legislative step

involves increasing the authorization for more auditors, investigators, compliance officers and support personnel as well as additional travel funds. We understand that some administrative changes within HEW have recently been undertaken with a view toward strengthening this surveillance component. The Education Subcommittee should determine whether those efforts suffice or whether they are merely cosmetic.

In addition, since there are no criminal penalties now being used by the Office of Education in prosecuting violators, it is suggested that criminal penalties be written into the law which would prohibit:

– The siphoning off of or allocation of grant funds for purposes not directly related to education, including entertainment, transportation of non-students, payments to non-students for non-educational services, and payments to federal, state or local officials intended to influence governmental action favorable to a school;

– False statements made to accreditation organizations;

– Fraudulent action of individuals which cause a default claim to be filed against the United States;

[p. 4736] – The payment of bribes to lenders to induce them to buy GSL loans; and

– The intentional destruction of records by any participants in the GSL program.

To provide a marketing unit for guaranteed student loans, Congress created the Student Loan Marketing Association, a quasi-governmental corporation, in 1973. Now, however, it is the opinion of the Department of Health, Education and Welfare that guaranteed student loans are not negotiable instruments and it is therefore questionable what useful function the Student Loan Marketing Association (SALLIE MAE) is serving.

Moreover, the enabling legislation did not require audit of SALLIE MAE by the General Accounting Office. Consideration should be given to requiring a GAO audit of SALLIE MAE, with a report to be prepared for Congress within six months.

For some time, HEW has proposed cutting the National Direct Student Loan Program and the Supplemental Educational Opportunity Grants Program. This proposal merits consideration if coupled with a broadening of the Basic Educational Opportunity Grant Program to pick up true hardship cases now being handled by SEOG. An alternative would be to use NDSL and SEOG programs only for students in higher-learning institutions, while terminating these programs for proprietary vocational schools, since this latter category is where most of the abuses have been found.

Before termination of any of these programs, however, a complete audit of the disposition of the funds should be completed. It is likely that such audits will show massive amounts of unaccounted-for federal monies.

In addition, there are many other problems in the program which could be corrected by new or revised

regulations or administrative procedures. Examples include the accreditation process, the composition and authority of boards making outright grants to schools, procedures whereby dropouts can be monitored, problems with present computer and record-keeping capabilities, and clarification of rights and obligations of lenders, students and the government. But one of the greatest criticisms we have of HEW is that they have not promulgated essential regulations to run the program properly. We believe it has reached the point where you might want to consider including in pertinent legislation a directive that HEW promulgate regulations in these and other specified areas with the imposition of a stringent time requirement.

[p. 4737] We hope these suggestions will be of some assistance to you in your examination of legislation in this important area. Please feel free to call upon us for any further assistance.

Sincerely,

/s/ _____
Sam Nunn, U.S.S.

/s/ _____
Charles H. Percy, U.S.S.

Legislative History

H. Rep. No. 102-447, 102nd Cong. 2nd Sess. vol. 4, p. 42-43 51 (1992), reprinted in 1992 U.S.C.C.A.N. p. 375-76, 384

Since the 1986 amendments, one guaranty agency has failed and the Department has informed the Committee that others are financially unstable. In order to monitor the financial sovency of guaranty agencies, the Secretary is authorized under H.R. 3553 to collect financial information annually from each agency. Based on the information available to him, the Secretary shall establish standards for the financial strength of guaranty agencies. Those agencies which do not meet the standards shall be subject to management plans. Any agency identified by the Secretary pursuant to these standards shall file a guaranty agency management plan which identifies management, investment, operational, and policy changes designed to improve the financial viability of the agency. Such plans shall be submitted to the Secretary and subject to his approval.

If an agency fails to file an acceptable management plan, or if it is determined by the Secretary not to be financially viable, H.R. 3553 requires the Secretary to do at least one of the following: (1) provide the agency with additional advance funds; (2) permit transfer or guarantees to another agency; (3) revoke the agency's reinsurance agreement at a specified date, thereby forcing the merger, consolidation, or termination of the agency; (4) transfer the guarantees to the Department of Education for the purpose of paying claims; or (5) take any other action the Secretary deems necessary to assure payment of default claims to lenders and avoid disruption of the student loan program.

***

Legislative History

The Committee heard much concern about the effect of guaranty agency failure upon the lenders' rights to have default claim paid. H.R. 3553 clarifies that in such a situation, the holder of loans insured by the insolvent guaranty agency may submit insurance claims directly to the Secretary for payment. The Committee intends such arrangements to continue only until the Secretary is satisfied that the loans have been transferred to a guarantor able to assume the outstanding insurance obligations.

H. Conf. Rep. No. 102-630, 102nd Cong. 2nd Sess. vol. 4, p. 451 (1992), reprinted in 1992 U.S.C.C.A.N. p. 556

The Senate bill, but not the House bill, provides that the unencumbered non-Federal portion of a guaranty agency's reserve fund shall not be subject to spend down.

The House recedes.

H. Conf. Rep. No. 103-213, 103rd Cong. 1st Sess. vol. 3, p. 455-56 (1976), reprinted in 1993 U.S.C.C.A.N. p. 1144-45

Reserve Funds

House bill

No provision.

Senate amendment

Section 422(g) allows the Secretary to require the return of all of the reserve funds of a guaranty agency in order

to ensure the proper maintenance of such agency's funds and assets.

Conference agreement

The House recedes with an amendment requiring that regulations for this provision be developed through negotiated rulemaking and that these regulations contain a provision for administrative due process. The amendment provides that the Secretary, in making a determination to direct a guaranty agency to return assets, shall make such determination based on standards developed through the negotiated rulemaking process and published by the Secretary in regulations, and that those standards shall include procedures for administrative due process. The conferees have included this language so that the Secretary and the higher education community will engage in a full and open discussion of this issue, and actively cooperate to develop these standards, however, the conferees wish to emphasize that this language is not intended to diminish the longstanding and judicially supported view that a guaranty agency's assets are dedicated to the loan programs and may not be used for unauthorized purposes. It is the conferees further intention that all references to guaranty agencies reserves contained in amendments to section 422 refer only to the "Federal portion" of such reserves.

APPENDIX J

DEPARTMENT OF HEALTH EDUCATION AND WELFARE

AGREEMENT FOR FEDERAL REINSURANCE OF LOANS PURSUANT TO 428 (c) OF THE HIGHER EDUCATION ACT OF 1965, AS AMENDED

WHEREAS, Student Loan Fund of Idaho, Inc. (hereinafter referred to as the "agency) has entered into an agreement with the U.S. Commissioner of Education (hereinafter referred to as the "Commissioner") pursuant to section 428(b) of the Higher Education Act of 1965, as amended (hereinafter referred to as the "Act") dated _____ ___ (hereinafter referred to as the "428(b) Agreement");

WHEREAS, the Agency has assured the Commissioner of its intention to continue to carry out a program of loan insurance under the 428(b) Agreement, which agreement is in full force and effect; and

WHEREAS, the Agency has assured the Commissioner that such Federal credit as is extended to the Agency under this agreement, through the Federal reinsurance of its insurance obligations to lenders is acceptable in lieu of cash in full satisfaction of any State law and regulations regarding the maintenance of the Agency's reserve funds;

NOW, THEREFORE, pursuant to the provisions of section 428(c)(1)(A) of the Act (excluding the provisions of

section 428(c)(1)(B) and (C)), it is mutually agreed as follows:

1. This agreement shall be construed in the light of, and all terms used herein shall have the same meaning as in, the Act and the Regulations promulgated thereunder. The Agency shall be bound by all changes in the Act or Regulations in accordance with their effective dates.

2. The Commissioner shall reimburse the Agency in an amount equal to 80 percent of the amount expended by it in discharge of its insurance obligations with respect to losses (resulting from the default of the student borrower or, in the case of loans made prior to December 15, 1968, resulting from the death or total and permanent disability of the student borrower) on the unpaid balance of principal and accrued interest of any insured loan with respect to which a portion of the interest is payable by the Commissioner under section 428(a) of the Act, or would be payable thereunder but for the borrower's lack of need.

3. All payments made by the Commissioner to the Agency pursuant to this agreement will be promptly deposited in or credited to the Agency's reserve fund, or if applicable, the reserve fund maintained for the purposes of section 422(c) of the Act.

4. The Agency shall establish and maintain such administrative and fiscal procedures as are necessary to ensure proper and efficient administration of its Student Loan Insurance Program. The Agency shall assure that due diligence (as described in regulations promulgated by the Commissioner, unless the Agency has established and disseminated its own specific standards for due diligence to be

submitted for approval in accord with section 9 of this Agreement) will be exercised by lenders In the making, servicing, and collecting of loans insured under its Student Loan Insurance Program and by the Agency in the collecting of defaulted loans which it holds. The Commissioner's execution of this Agreement shall not be construed as indicating his acceptance of any procedures as may currently be or previously have been employed by the Agency.

5. In connection with any claim for payment on a loan re-insured pursuant to this Agreement, the Agency shall assure the Commissioner that (a) the terms of such loan comply with all Agency, State-and Federal requirements, (b) that all reasonable efforts have been made to collect the loan, and (c) the loan is in default or, with respect to loans made prior to December 15, 1968, that the borrower is deceased or it totally and permanently disabled (as defined and determined in the Act and the regulations promulgated thereunder).

6. The Agency may, if authorized by regulations promulgated under the Act, allow forbearance for the benefit of the student-borrower as may be agreed upon by the parties to the loan and approved by the Agency.

7. If, after the Commissioner has made payment under this agreement, any payments are made by the borrower in discharge of the loan obligations (including any payments of interest, accruing on such loan after payment by the Commissioner), there shall be paid over to the Commissioner such proportions of the amounts of such payments as is determined (in accordance with section 428(c)(6) of the Act) to represent his equitable share thereof. The Agency shall submit such payments due the Commissioner within sixty days

of the receipt of the payments on the loan. Unless the Commissioner provided otherwise by regulations, amounts paid by the borrower on the loan shall be first applied in reduction of principal owing on the loan.

8. The Commissioner shall make payments pursuant to this agreement at such times, in such manner and on the basis of such documentation as he may from time to time prescribe. The Commissioner may set off amounts payable to him by the Agency against amounts payable by him to the Agency.

9. The Agency shall submit reports to the Commissioner at such times and in such manner as he may reasonably prescribe concerning the status of the reserve fund and the operation of the Agency's Student Loan Insurance Program. The Agency shall keep such records as may be necessary to make such reports, and shall afford access thereto at any reasonable time to the Commissioner or other agencies of the Federal Government designated by the Commissioner to assure the correctness and verification of such reports.

In addition, the Agency shall submit to the Commissioner upon request any of the forms, procedures or other materials used in the operation of its Student Loan Insurance Program. The Agency shall also submit to the Commissioner for his approval and prior to their adoption any forms, procedures, regulations, or other materials which the Agency proposes to adopt or revise and which substantially affect the operation of its Student Loan Insurance Program, including any proposed arrangement with a private nonprofit loan insurance agency for the administration of the Agency's Student Loan Insurance Program.

10. Nothing in this agreement shall be construed to require collection of the amount of any loan by the lender or the Agency from the estate of a deceased borrower, or from a borrower found by the lender or the Agency to have become totally and permanently disabled (as determined in accordance with Federal regulations).

11. The Commissioner's obligations to make payments, as provided for in this Agreement, shall extend only with respect to loans insured by the Agency prior to termination of this agreement or prior to the expiration of the authority provided in the Act.

12. This Agreement may be terminated by either party upon not less that 60 days written notice to the other party, except that the Commissioner may terminate this Agreement only for cause. Termination shall not affect obligations incurred under this Agreement by either party before the effective date of termination. If termination is effected by the Commissioner, it will not become final until the Agency has been afforded reasonable notice and an opportunity for a hearing, except that the Commissioner may suspend this Agreement pending the outcome of the hearing if he determines that such action is necessary in order to prevent substantial harm to Federal interests.

13. If the Commissioner finds that any of the assurances or representations made by the Agency in connection with this Agreement are incomplete or incorrect in any material respect or that there has been a failure by the Agency to comply with any of the provisions of this Agreement or applicable Federal law or regulations, he may take such action short of termination as may be necessary to

protect the interests of the United States. Such action may include withholding payments to be made to the Agency (or to lenders whose loans are insured by the Agency) until adequate documentation thereof is provided or requiring that the Agency reimburse the Commissioner for any payments made, or any payments which the Commissioner has become obligated to make, as a result of the Agency's making such incomplete or incorrect statements or violating such provisions of this Agreement or applicable Federal law or regulations.

14. No member of or delegate to Congress; or resident Commissioner, shall be admitted to any share or part of this agreement, er to any benefit that may arise therefrom; but this provision shall not be construed to extend to this agreement if made with a corporation for its general benefits.

IN WITNESS WHEREOF, this Agreement has been executed by the duly authorized representative of the Agency and in the name of and on behalf of the Commissioner, by the undersigned official.

Student Loan Fund of Idaho, Inc.
Name of Agency

Date: June 27, 1978

By /s/ _____
Title Executive Director

Attest: /s/_____
Title Vice President

Agreement for Federal Reinsurance of Loans

United States Commissioner
Of Education

Date: July 20, 1978

By /s/ _____
Peter K.U. Voigt
Title Acting Director, Division of Policy and Program Development

APPENDIX K

DEPARTMENT OF HEALTH EDUCATION AND WELFARE

SUPPLEMENTAL GUARANTY AGREEMENT FOR FEDERAL REINSURANCE OF LOANS HIGHER EDUCATION ACT OF 1965, AS AMENDED

WHEREAS, Student Loan Fund of Idaho, Inc. (hereinafter referred to as the "Agency") has entered into an agreement with the United States Commissioner of Education (hereinafter referred to as the "Commissioner") pursuant to section 428(b) (hereinafter referred to as the "428 (b) Agreement") of the Higher Education Act of 1965, as amended (hereinafter referred to as the "Act"), entitling students who receive loans which are insured by the Agency to have made on their behalf the payments provided in Section 428(a) of the Act; and

WHEREAS, the Agency has entered into an Agreement with the Commissioner pursuant to Section 428 (c) (1) (A) of the Act (hereinafter referred to as the "428 (c) Agreement"), providing for Federal reimbursement of a percentage of losses incurred by the Agency which result from the default of borrowers receiving student loans insured by the Agency; and

WHEREAS, the Agency assures the Commissioner of its intention to continue to carry out a program of loan insurance under the 428(b) Agreement, which agreement s are

in full force and effect; and

WHEREAS, the Agency assures the Commissioner that, with respect to so much of any loan insured under the Agency's Student Loan Insurance Program as may be guaranteed by he Commissioner pursuant to this Agreement and to Section 428A of the Act, the undertaking of the Commissioner under this Agreement is acceptable in full satisfaction of any State law or regulation requiring the maintenance of the Agency's reserve fund; and

WHEREAS, the Agency assures the Commissioner that its Student Loan Insurance Program meets, and will continue to meet, the requirements of Section 428A (a) (1) of the Act; and

WHEREAS, the Agency assures the Commissioner that it is and will continue to be, otherwise in compliance with the Act and any regulations promulgated pursuant to the Act;

NOW, THEREFORE, pursuant to the provisions of section 428A of the Act, it is hereby agreed by and between the parties as follows:

1. Based on the above set forth assurances, the commissioner determines that the Agency is eligible to enter into this Supplemental Guaranty Agreement.

2. The Commissioner shall reimburse the Agency, at such times, in such manner, and on the basis of such documentation as he may from time to time reasonably prescribe, with respect to losses (resulting from the default of student borrowers or, in the case of loans made prior to December 15,

1968, resulting from the death or total and permanent disability of student borrowers) on the unpaid balance of the principal and accrued interest of any student loan insured under the Agency's Student Loan Insurance Program in an amount equal to one hundred per centum (100%) of the amount of losses incurred by the Agency tn the discharge of its insurance obligations incurred under its Student Loan Insurance Program, except that:

(a) if, for any Federal fiscal year, the amount of such reimbursement payments by the Commissioner pursuant to this Agreement-exceeds five per centum (5%) of the loans which are insured by the Agency under its Student Loan Insurance Program and which were in repayment at the end of the preceding fiscal year, the amount to be paid as reimbursement under this Agreement for such excess shall be equal to-ninety per centum (90%) of the amount of such excess; and

(b) if, for any Federal fiscal year the amount of such reimbursement payments exceeds nine per centum (9%) of such loans, the amount to be paid as reimbursement under this Agreement for such excess shall be equal to eighty per centum (80%) of the amount of such excess.

For purposes of this Agreement, the amount of loans of the Agency which are in repayment shall be the original principal amount of loans made by a lender which are insured by the agency reduced by (i) the amount the Agency has been

required to pay to discharge its insurance obligations under the Act, (ii) the original principal amount of loans insured by it which have been fully repaid, and (iii) the original principal amount insured on those loans for which payment of the first installment of principal has not become due pursuant to Section 428 (b) (1) (E) of the Act or for which the first installment need not be paid pursuant to Section 428(b) (1) (M) of the Act.

3. All payments made by the Commissioner to the Agency pursuant to this Agreement will be promptly deposited in or credited to the Agency's reserve fund.

4. The Agency shall establish and maintain such administrative and fiscal procedures as are necessary to assure proper and efficient administration of its Student Loan Insurance Program. The agency shall assure that due diligence(as described in regulations promulgated by the Commissioner, unless the Agency has established and disseminated its on comparable standards for due diligence which have been approved in accordance with Section 6 of this Agreement) will be exercised by lenders in making, servicing and collecting loans insured under its Student Loan Insurance Program and by the Agency in collecting defaulted loans which it holds. The Commissioner's execution of this Agreement shall not be construed as indicating his acceptance of any procedures that may currently by or previously have been employed by the Agency.

5. In connection with any claim for payment on a loan reinsured Pursuant to this Agreement, the Agency shall assure the Commissioner that (a) the terms of such loan comply with all Agency, State, and federal requirements, (b) all reasonable

efforts have been made to collect the loan, and (c) the loan is in default or, with respect to loans made prior to December 15, 1968, the borrower is deceased or is totally and permanently disabled (as defined and determined in the Act and the regulations promulgated thereunder).

6. The Agency shall submit reports to the Commissioner at such times and in such manner as he may reasonably prescribe concerning the status of the reserve fund and the operation of the Agency's Student Loan Insurance Program. The Agency shall keep such records as may be necessary to make such reports and shall afford access thereto at any reasonable time to the Commissioner or other agencies of the Federal government designated by the Commissioner to assure the correctness and verification of such reports.

In addition the Agency shall submit to the Commissioner upon request any of the forms, procedures, or other materials used in the operation of its Student Loan Insurance Program. The Agency shall also submit to the Commissioner for his approval and prior to their adoption any forms, procedures, regulations, or other materials which the Agency proposes to adopt or revise and which substantially affect the operation of its Student Loan Insurance Program, including and proposed arrangement with a private non-profit loan insurance agency for the administration of the Agency's Student Loan Insurance Program.

7. If, after a payment has been made by the Commissioner pursuant to this Agreement with respect to any loan, any payments are made to the Agency in discharge of the obligations incurred by the borrower with respect to such loan (including any payments of interest accruing on any such

loan after such payment by the Commissioner), there shall be paid over to the Commissioner (for deposit in the fund established by Section 431 of the Act) such portion of the amount of such payment as is determined (in accordance with regulations prescribed or to be prescribed by the Commissioner) to represent his equitable share thereof. 0therwise, there shall be no subrogation of the United States to the rights of the Agency. Except as the Commissioner may by regulation or otherwise provide, amounts so paid by a borrower on such loan shall be first applied to the reduction of principal owing on such loan. The Agency shall submit payments due the Commissioner pursuant to this section within 60 days of the receipt of such payments. The Commissioner may offset the amounts payable to him by the Agency against amounts payable by him to the Agency.

8. The Agency may, as authorized by regulations promulgated under the Act, allow forbearance for the benefit of the student borrower as may be agreed upon by the parties to the loan and approved by the Agency.

9. The Commissioner's obligation to make payments, as provided for in this Agreement, shall extend only with respect to loans insured by the Agency prior to the expiration of the authority provided in the Act. This Agreement is subject to annual renegotiation; provided, however, that until 60 days (or such longer period as the Commissioner may permit) after the Commissioner commences such renegotiation, this Agreement shall remain in effect so as to provide Federal reinsurance benefits to the greatest extent possible under the Act as to all student loans guaranteed by the Agency.

10. This Agreement may be terminated by either party upon not less than 60 days written notice to the other party, except that the Commissioner may terminate this Agreement only for cause. Termination shall not affect obligations incurred under this Agreement by either party before the effective date of termination. If termination is effected by the Commissioner, it will not become final until the Agency has been afforded reasonable notice and an opportunity for a hearing, except that the Commissioner may suspend this Agreement pending the outcome of the hearing if he determines that such action is necessary in order to prevent substantial harm to Federal interests.

If the Commissioner finds that any of the assurances or representations made by the Agency in connection with this Agreement are incomplete or incorrect in any material respect or that there has been a failure by the Agency to comply with any of the provisions of this Agreement or applicable Federal law or regulations, he may take such action short of termination as may be necessary to protect the interests of the United States. Such action may include withholding payments to be made to the Agency until adequate documentation therefor is provided or requiring that the Agency reimburse the Commissioner for any payments made, or any payments which the Commissioner has become obligated to make, as a result of the Agency's making such incomplete or incorrect statements or violating such provisions of this Agreement or applicable Federal law or regulations.

11. This Agreement shall be construed in light of the Act and the regulations thereunder.

12. This Agreement shall apply to all reinsurance payments made by the Commissioner after June 27, 1978.

Student Loan Fund of Idaho, Inc.
Name of Agency

Date: June 27, 1978

By /s/ _____
Its Executive Director
And /s/ _____
Its Vice President

Date: July 20, 1978

By /s/ _____

APPENDIX L

UNITED STATES DEPARTMENT OF EDUCATION

[Dated June 19, 1986]

Briefing Document on Guaranteed Student Loan Program Guarantee Agency Reserves

TO: William J. Gainer, Associate Director
Human Resources Division
U.S. General Accounting Office

FROM: Assistant Secretary for
Postsecondary Education

Subject: Briefing Document on Guaranteed Student Loan Program Guarantee Agency Reserves

Thank you for providing a copy of the above referenced report to us for review. Several offices within the Department of Education have reviewed the report, including the Office of Planning, Budget and Evaluation, the Office of Postsecondary Education and the Office of Legislation. The Department commends the GAO for developing a high quality report in a short period of time. We believe the general thrust of GAO's analysis and recommendations will be helpful to the Department and the Congress, especially during this period of reauthorization of the Higher Education Act.

We believe it is important at the outset to clarify the general intent of the GAO in its analysis of the reserve fund needs of the guarantee agencies. In our view, GAO's task was to determine appropriate maximum reserve levels in relationship to the probable requirements encountered by the guarantee agencies for the use of such reserve funds (e.g., to cover the costs associated with the time delay between an agency's making claims payments to lenders and receiving reinsurance payments for such claims from the Department of Education). This task, therefore, would not encompass a broad measure of an agency's "solvency," per se, since solvency is based on numerous other factors (e.g., alternative sources of funding, potential maximum liabilities, etc.) many of which are not related to the practical level of reserves needed to assure a smooth flow of agency operations. Thus, the Department views the guidelines proposed by GAO as approximate measures of reserves required to cover probable agency needs for such funds--not as measures of reserves required to ensure solvency under potential liabilities.

This Administration has sought to address the problem of more appropriate levels of agency reserves through several means, notably in our reauthorization proposal to require return of all Federal advances. Other proposals, such as reduced reinsurance rates, would address this problem, as well as encourage improvements in default prevention and collection and in administrative cost efficiency. We continue to urge the Congress to enact these legislative changes to improve the long-term operation of the GSL program.

However, we are supportive of the GAO's proposed criteria for establishing maximum guarantee agency reserve levels on the basis of: (1) a percentage of default claims paid during the

prior fiscal year; (2) a percentage of the original principal amount of outstanding loans, and (3) $500,000 as a minimum dollar amount for reserves.

We suggest that the first measure should be set at 40 percent of claims paid in the prior year and the second at 0.3 percent of outstanding loans. The GAO report indicates that no agency's negative cash flow exceeded both of these levels during Fiscal Years 1984 and 1985. The maximum reserve level established by these two criteria will increase on an annual basis as the amount of default claims paid and loan volume increase. Thus, reserve fund maximums pegged at either 40 percent of default claims paid or 0.3 percent of outstanding loans should provide sufficient reserves to meet any reasonable contingencies in subsequent years since the levels of liabilities and reserve funds should rise concurrently. Furthermore, we believe that an overly generous criterion with respect to default claims paid would marginally reduce incentives for guarantee agencies to take stronger measures to prevent and reduce defaults. In addition, the $500,000 minimum provides a reliable floor for very small agencies.

We are concerned that agencies not be permitted to manipulate their reserve fund balances and thus avoid repaying their advances or having their reinsurance payments withheld by using monies from their reserve funds for non-program purposes (see attachment citing abuse practices in this area). Although we have issued proposed regulations which would prohibit such practices, we feel strongly that the Congress should legislatively prohibit such inappropriate uses of agency reserve funds.

We are also concerned with possible agency manipulation of reserve fund levels to avoid repaying advances or having reinsurance payments withheld by reducing or eliminating the insurance premium charged to borrowers. The insurance premium is the agencies' largest source of income. In the past, the Department has favored allotting agencies discretion in setting the amount of their own insurance premiums. However, in the context of the GAO's recommended criteria, we are concerned about the potential for abuse which could prove costly to the taxpayers. Therefore, we recommend that the agencies be required to charge a minimum insurance premium of one percent per year of the unpaid balance of the loan during the In-school and grace periods--the "maximum practical amount" cited by the GAO. This is also the typical amount currently charged by the majority of agencies. In essence, we are proposing that Congress legislate the typical current practice as a minimum for all agencies.

The proposal for reducing excess reserves by withholding reinsurance payments is commendable. However, we would like to stress that this proposal should not be viewed as an alternative to pending proposed legislation, designed to improve an agency's default prevention and collection efforts by decreasing the reinsurance rates based upon the agency's default and collection experience. The withholding of reinsurance payments can be effective in reducing excess reserves over the next few years. However, once an agency's reserves have been limited to a reasonable level, no strong financial incentive will exist for the agency to reduce defaults and improve collections. Our proposals for reduced reinsurance rates, loan counseling and other program changes would effect long-term improvements in default prevention and collection.

While we fully support the proposal to require agencies to return Federal advances as determined under GAO's proposed criteria, we remain committed to the proposition that agencies no longer need Federal advances and that such monies should be returned immediately. Therefore, we suggest a timetable for immediate implementation be incorporated into this proposal to ensure that the problem of excessive reserve funds be addressed and that advances are returned before Fiscal Year 1988 as currently mandated. We strongly suggest that the effective date should be established to assure that Fiscal Year 1986 will be the first baseline year used. In addition, we recommend that the GAO include in its report a recommendation for repeal of the authority for making additional Federal advances currently found in Section 422(c) of the Act.

We believe that, after these provisions have been in effect for one year, their effectiveness should be thoroughly evaluated to determine if the criteria for setting the maximum reserve levels are appropriate.

Again, thank you for allowing us to review and comment on the draft report. We appreciate the opportunity to work with the GAO in a cooperative effort to make more efficient use of Federal funds.

/s/ _____
C. Ronald Kimberling

Attachment

GAO Report - August 1986

Use of GSL Reserve Fund Monies
for Non-CSL Purposes

The reserve fund established by a guarantee agency is intended to support the agency's loan guarantees. The Federal government advances funds to an agency on certain conditions. Included among those conditions is that the agency's reserve fund may be used only for specific purposes related to the GSL program. Once the Federal monies are returned to the Federal government the use of the reserve fund is no longer restricted by Federal regulations.

Several agencies that have repaid their Federal advances have immediately used their reserve funds for purposes which are completely unrelated to the GSL program. For example:

- The New Jersey Higher Education Assistance Authority returned $6.7 million in Federal advances earlier this year. Of the monies remaining in the reserve fund, $15 million were transferred to a dedicated fund under the control of the State Board of Education, and up to $10 million were transferred to an "Educational Loan Development Fund," to be used for unspecified purposes.

- The Oregon State Scholarship Commission returned their Federal advance and subsequently transferred $1.6 million of the monies remaining in the reserve fund to a State grant program.

APPENDIX M

STUDENT LOAN FUND OF IDAHO, INC.

[Dated April 22, 1994]

Letter from Carrol Lee Lawhorn to Richard W. Riley

Richard W. Riley
Secretary of Education
U.S. Department of Education 400 Maryland Avenue,
Suite 4181
Washington, D.C. 20202

Dear Secretary Riley:

Provisions of the Omnibus Budget Reconciliation Act of 1993 which begin to impact the student loan programs on July 1, 1994 will have such a negative financial impact that our organization cannot prudently continue to participate.

Please accept this letter as the 60 day written notice of termination required in our agreements. We will guarantee no additional loans under your programs after June 30, 1994.

Sincerely,

/s/ _____
Carrol Lee Lawhorn
Executive Director
CLL:ssg

APPENDIX N

UNITED STATES DEPARTMENT OF EDUCATION

[Dated September 20, 1994]

Letter from Larry Oxendine to Carrol Lee Lawhorn

Mr. Carrol Lee Lawhorn
Director
Student Loan Fund of Idaho, Inc.
P.O. Box 730
Fruitland, ID 83619

Dear Mr. Lawhorn:

In a letter dated April 22, 1994, you informed the Department of Education (Department) that the Student Loan Guaranty Fund of Idaho, Inc. (SLFI) would not guarantee any additional loans under the Federal Family Education Loan Program (FFELP) effective July 1, 1994. The Department designated the Northwest Education Loan Association (NELA) as the new designated guarantor for Idaho to ensure that students in Idaho continue to have access to FFELP loans. As part of the transfer of authority from SLFI to NELA, your agency was directed to transfer its outstanding loan portfolio and the guaranty agency reserve fund to NELA. SLFI has failed to comply with those directions.

During June 1994, the Department's Office of Inspector General began a review of SLFI's financial records in preparation for the transfer of responsibility to NELA. That review found that while SLFI intended to transfer certain reserve funds to NELA, it also intended to retain control over other Federal assets. SLFI apparently asserts that the assets maintained in an "Operating Fund" are not Federal property. On September 13, 1994, you confirmed this statement of SLFI's position in a conversation with me when I again directed you to transfer all Federal property to NELA.

SLFI's position is contrary to law. As you know, §422(g) (1) of the Higher Education Act of 1965, as amended (HEA), 20 U.S.C. §1072(g) (1), provides that the reserve funds and assets of the guaranty agencies are property of the United States to be used in the operation of the FFELP or the Federal Direct Student Loan Program. The funds maintained in SLFI's "Operating Fund" are funds accruing from SLFI's participation in the FFELP and funds provided directly by the Department to support SLFI's guaranty agency activities. Therefore, the funds maintained in SLFI's Operating Fund are part of SLFI's reserve fund and must be transferred to NELA.

Your agency has improperly delayed the completion of the transfer of responsibility and guaranty agency assets from SLFI to NELA. In light of this delay, the Department is taking the following actions:

1. Under the authority of §§422(g) and 428(c) (9) of the HEA, 20 U.S.C. §§1072(g) and 1078(c) (9), the Department directs SLFI to complete the transfer of its assets to NELA within 30 days of the date of this letter -- this transfer must be complete by October 20, 1994. This transfer

must include the transfer of all legal ownership and control of SLFI's assets to NELA, including: defaulted loans; outstanding guarantees; any and all funds, in whatever form; SLFI's "Reserve Fund"; SLFI's "Operating Fund"; and all physical assets wholly or partially owned by SLFI.

2. Within 10 days of the date of this letter, September 30, 1994, SLFI must send a letter to NELA, with a copy to the Department, confirming that the transfer will occur by October 19 and explaining how the transfer of assets and loans will occur.

3. Since SLFI is closing its operations in the FFELP, only limited use of the funds and assets is needed. To ensure that the Federal property held by SLFI is not improperly used or dissipated during the transfer period, the Department hereby directs SLFI to cease and desist from any activities involving the commitment, expenditure, use or transfer of any funds or assets held by SLFI in its Reserve Fund, Operating Fund or in any other account, without prior approval from the Department. See §§422(g) (1) (C) and 422 (g) (2) (B) of the HEA, 20 U.S.C. §§1072(g) (1)(C) and 1072(g)(2)(B). Prior approval will not be required for normal personnel expenditures including payment of salary and benefits to non-executive personnel. However, any payments to the Director of SLFI or members of the Board of Directors must be preapproved by the Department. To receive preapproval for expenditures please contact Jerry Turner of my staff at 202-708-9465.

The requirement for preapproval is effective immediately on your receipt of this letter and remains in effect until changed by the Department.

4. In principle, the Department is willing to permit SLFI to use its reserve funds to pay severance benefits to employees who stay with SLFI for as long as their services are required and who are not subsequently employed by NELA. Any such severance pay must be preapproved by the Department under paragraph 3 above.

The Department is very disappointed by SLFI's continued refusal to comply with its legal obligations. I can assure you that the Department is ready to take any and all appropriate steps to protect the Federal interest in the assets and funds maintained by SLFI for the FFELP. In this respect, I remind you that under §422(g) (3) of the HEA, 20 U.S.C. §1072(g)(3), violation of the directives included in this letter may result in initiation of criminal proceedings under §490 of the HEA, 20 U.S.C. §1097.

Sincerely,

/s/ _____
Larry Oxendine
Acting Director
Guarantor and Lender Oversight Staff

cc: Carl Donovan
Northwest Education Loan
Association